The Economist

Six experts on America's spies
BY INVITATION: PAGES 30-31

Mexico's wounded Fox
PAGES 11 AND 32

Rebellion in Hong Kong
PAGES 10 AND 35

Rethinking corporate strategy
PAGES 61-63

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The Americas
Asia
Middle East & Africa
Europe
Britain
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Cities Guide

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BUSINESS
Management Reading
Business Education
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PEOPLE
Obituary

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Style Guide

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Currencies
Big Mac Index

DIVERSIONS

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Mobile Edition
RSS Feeds

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Country Briefings Go
Audio interviews Go
Classifieds Go

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Fighting terrorism
Unjust, unwise, unAmerican

Hong Kong and China
Rebellion

Mexico's congressional election
Wounded and at bay

Asian currencies
Re-orientation needed

WMD and Iraq
Artificial intelligence?

Letters

On Howard Dean, cosmetics, Canada's oil sands, tax and leisure, Alan Greenspan, education, stars and stripes, Iraq's nuclear-weapons programme

Special Report

150 years after Commodore Perry
Japanese spirit, western things

United States

Foreign policy and domestic politics
And it used to be such a pleasure

Telling it to Iran
Prodding the clerics

Not enough houses in California
Homeless masses

Dealing with al-Qaeda suspects
A necessary evil?

The reaction from abroad
Just don't kill them

Lexington
Get me to the church on time

The Americas

Mexico's congressional election
Putting the brakes on change

Argentina's armed forces
Past crimes

Venezuela
Another Cuba?

Campaign finance in Canada
Closing the private purse

Bolivia
Fire in the Andes

Award

Asia

Hong Kong and China
In the dock

China
Boom town blues

Japan's economy
A bit of bounce

Television in India
A clearer picture

Sri Lanka
Rescuing the peace

Australia
Drying out

Business

Mergers
The return of the deal

Aluminium and antitrust
French twist?

Corporate finances
Less stretched, for now

Expensing share options
Out of options

Mobile telecoms
Doing the walkie-talkie

Beer innovation
The Eagle has landed

The Volkswagen Beetle
The last love bug

Face value
In praise of trial lawyers

Special Report

Corporate strategy
Who gets eaten and who gets to eat

Finance & Economics

Asian currencies
Fear of floating

Government bonds
Letting off steam

Bank Austria and Hypovereinsbank
Running repairs

Development
Years of plenty?

Wall Street research
Shortage of prophets

Asbestos litigation
Hatched, but not despatched

Economics focus
The euro, trade and growth

Science & Technology

Deep-vein thrombosis
Causing trouble

DVDs
This movie will self-destruct

Detecting malingerers
Hidden truths

The space shuttle accident
Foam alone

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Mathematics
Riemann's riddle

The history of Japan
Tokyo rose

German cinema
Auf Wiedersehen, pet

European integration
A new hymn sheet

Thomas Jones
Perfection in miniature

The travelling toads
Crocs crocked

Middle East & Africa

George Bush visits Africa
Making new friends, gingerly

Algeria's Islamist leaders
Still shackled

South African census
Who are we?

Local democracy in Iraq
Tiny steps in the dance

Iran's nuclear programme
Enriching

Palestinians in Iraq
Back in a tent

Europe

Russia
Power struggle in the Kremlin

Chechen suicide bombers
The black widows' revenge

A referendum in Corsica
A worrying result

A German scandal
An underlying theme?

Turkey and the United States
A partnership at risk?

Greece's government
A big clean-up is promised

Charlemagne
Burlesquoni

Britain

Intelligence and Iraq
The war isn't over for Tony

Iraq, Niger and uranium
Spies fall out

Manufacturing
The lessons of a closure

Squabbling Anglicans
Unholy orders

War stories
Blair's biscuits

Public services
Hooked on targets

Transport
Muddle of the roads

Interest rates
King's first cut

Aircraft noise
Dawn chorus

Bagehot
Tone alone

Political thriller
Kabul bounty

Obituary

Antonio Fortich

Economic and Financial Indicators

Overview

Output, demand and jobs

Prices and wages

Portfolio poll

Money and interest rates

The Economist commodity price index

Stockmarkets

Trade, exchange rates and budgets

The world's top banks

Emerging-Market Indicators

Overview

Economic freedom

Economy

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Politics this week

Jul 10th 2003
From The Economist print edition

America abroad

Reuters

George Bush toured **Africa**, discussing trade, aid and security matters with several African presidents. He again instructed Liberia's president, Charles Taylor, to resign and go into exile, but did not decide whether to send American troops to restore peace to Liberia.

See article: George Bush's African safari

A **Baghdad municipal council** was inaugurated, as part of the American plan to set up local advisory councils. Saddam Hussein's voice was heard again when Arab satellite TV stations played tapes, reckoned to be authentic though the time of recording was unknown, calling on Iraqis to resist the occupying powers. The violence continued, with several American soldiers and a British freelance journalist killed.

See article: The inauguration of Iraqi local councils

After Israel had approved the release of only a handful of the 6,000 Palestinian prisoners it holds, **Mahmoud Abbas** came under fierce Palestinian pressure for making too many concessions. He threatened to resign both as Fatah leader and prime minister.

Islamists and government supporters were the victors in **Kuwait's** all-male election. Liberals and their supporters took only three seats in the 50-seat parliament, a sharp drop from 14 seats in the outgoing parliament.

A general strike ended in **Nigeria** after the government reduced its recent increase in the price of petrol. Union leaders claimed that several strikers had been killed; the police denied it.

The Gray vote

A campaign to recall Governor Gray Davis of **California** claimed it had assembled enough signatures to force a referendum on removing him.

Another top **Bush economic official** resigned. Peter Fisher, the Treasury's under-secretary for domestic finance, will leave in October. In an attempt to mitigate understaffing at the top, the department nominated four senior officials, including a deputy secretary, Susan Schwab.

The Bush administration admitted that the president had relied on faulty information when he accused Saddam Hussein of trying to buy **uranium** from Africa. British intelligence officials were also cross that he attributed this information to them.

See article: Another intelligence dispute

Donald Rumsfeld admitted that the cost of keeping America's 145,000 **troops in Iraq** was $3.9 billion a month—double the previous estimate.

See article: Diplomacy and its political effects

Six people died and another eight were wounded when a white worker with allegedly racist leanings went on a **shooting spree** at a Mississippi factory.

A fortnight late, America's latest **Mars** rover, dubbed *Opportunity*, was launched from Cape Canaveral. It should arrive at its destination early next year.

Candelight concession

AP

About 50,000 people took part in a candlelit vigil in **Hong Kong**, calling for universal suffrage in the territory and the sacking of its chief executive, Tung Chee-hwa. Earlier, after public protests, Mr Tung had postponed the passage of an anti-subversion bill.

See article: Hong Kong and China

The government of the **Solomon Islands** voted to accept an international peacekeeping force led by Australia.

At least 400 people were drowned when an overcrowded ferry sank in the Meghna river at Chandpur, **Bangladesh**. About 200 people survived.

South Korea's intelligence service renewed fears about **North Korea's** nuclear plans by confirming that its neighbour had reprocessed a number of spent fuel rods and had tested devices to trigger atomic explosions.

Laos freed and deported two European journalists and an American who had been sentenced to 15 years in jail after being accused of involvement in the death of a village guard.

Slightly foxed

AP

In a big setback for **Mexico's** president, Vicente Fox, his National Action Party lost ground in a mid-term election for the lower house of Congress that was marked by a low turnout. The formerly ruling Institutional Revolutionary Party gained seats, consolidating its position as the largest party in Congress.

See article: Mexico's congressional election

Argentina's new president, Néstor Kirchner, told stony-faced army chiefs that they should “accept responsibility” for their actions during the 1970s “dirty war” against guerrillas. The government plans to repeal a decree barring the extradition of army officers in human-rights cases.

See article: Past crimes

In **Brazil**, an indefinite strike by civil servants against a bill to reform pensions gained modest support. But a proposal to dilute the reform was being considered by officials.

Terror in Moscow

AFP

Two female **Chechen** suicide-bombers killed at least 16 people, including themselves, at a rock concert on the outskirts of Moscow, in protest against Russia's campaign to suppress the separatist rebellion in Chechnya.

See article: Why Chechen suicide bombers are attacking Moscow

President Vladimir Putin seemed to be warning **Russia's** tycoons to keep out of politics (unless on his side) when Platon Lebedev, one of the main

shareholders in Russia's biggest oil company, Yukos, was arrested on a charge of illegally acquiring shares in another company in 1994; Yukos's president, Mikkail Khodorkovksy, was briefly questioned by the police.

See article: A new power struggle in the Kremlin

After last week's remark by Italy's prime minister, **Silvio Berlusconi**, likening a German MEP to a Nazi concentration-camp guard, one of his ministers added fuel to the row by complaining about German tourists' allegedly aggressive behaviour on Italy's beaches. Germany's chancellor, Gerhard Schröder, cancelled the summer holiday he had planned to spend in Italy.

See article: Is Italy really becoming more Eurosceptical?

Voters in France's Mediterranean island of **Corsica** narrowly rejected a plan for limited autonomy that had been put to a referendum.

Greece's prime minister, Costas Simitis, sacked the old-guard secretary-general of his ruling Pan-Hellenic Socialist Movement and replaced him with a moderniser. He also declared war on corruption.

See article: Greece's prime minister makes war on corruption

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Business this week

Jul 10th 2003
From The Economist print edition

French twist?

Pechiney reacted with Gallic *froideur* to an unsolicited *euro*3.8 billion ($3.8 billion) bid from Canada's **Alcan**, a rival aluminium firm, calling it unfriendly, unwanted and insufficient. Together they would challenge America's Alcoa for world leadership. But European competition watchdogs may object. Meanwhile, Pechiney is casting about for a suitable “white knight”.

See article: Aluminium to test bureaucrats' mettle

EMC, a data-storage-equipment firm, offered $1.3 billion in shares to buy **Legato Systems**, a rival software-storage company.

Trucker Yellow, a leading American haulage company, agreed to pay $966m for a rival, **Roadway**. Long-haul truckers have suffered as the faltering economy hit business and created overcapacity. Consolidated Freightways, another rival, closed last year.

Running out of options

Microsoft announced that it would abandon the practice of rewarding its staff with stock options. The company helped to make options the turbocharger of the high-tech industry, creating hundreds of millionaires along the way. It will now use real shares to pay workers—and will acknowledge the cost of the shares in its accounts.

See article: Microsoft abandons share options

ArvinMeritor, a top American car-parts maker, announced it would make a $2.2 billion hostile bid for **Dana,** a competing car-parts firm. Cost pressures on the industry have prompted carmakers to use fewer suppliers and seek general economies. Dana's shares surged on the news.

America's number-two and -three tobacco firms discussed a link-up, according to reports. **R.J. Reynolds** and **Brown & Williamson**, part of British American Tobacco, would together have a 33% market share in America, the better to fight off threats from low-cost brands, litigation and the marketing might of Altria, Philip Morris's parent company.

Altria's shares fell after an American court began a hearing into whether a judge had been entitled to cut a bond of $12 billion. The firm was required to hand over the bond while appealing against a ruling that it must pay smokers $10 billion for deceiving them about the danger of the habit.

Luc Vandevelde, a former chief executive of **Marks & Spencer** and now chairman, has agreed to be paid in shares after he makes his role part-time in September. He called the arrangement a “vote of confidence” in the company's ability to create shareholder value. He will earn over £500,000 ($815,000) a year at the current share price.

A French court froze a *euro*20m ($23m) severance package awarded to **Jean-Marie Messier**, former boss of Vivendi Universal. The French media giant's shareholders have described as “scandalous” the reward for the man whose disastrous acquisitions strategy had saddled the firm with vast debts.

Reports emerged that **Crédit Lyonnais** was offered a settlement to a long-running fraud investigation by American prosecutors. In return, the French bank would be required to pay a fine of up to $600m and

plead guilty to at least one criminal charge. Crédit Lyonnais may not accept the latter condition.

Plough in a furrow

Schering-Plough gave warning that second-quarter profits would be below forecasts and that profits for the year would fall by 66% compared with 2002. Merck, a potential buyer of the American drug firm, said that it was not planning to make a bid. Schering-Plough's shares fell.

SARS, blamed by all manner of firms around the world for recent losses, provided a surprise profit for one. **Sohu.com**, a leading Chinese internet portal, reaped the rewards as millions went online at home, rather than run the risk of contracting the disease after a trip outside.

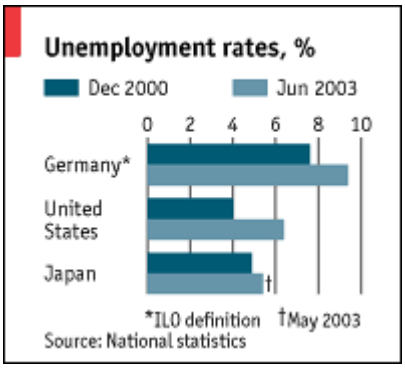
Rothschild united

The English and French branches of the **Rothschild** family unveiled a restructuring that will unite the two arms of the bank under Baron David de Rothschild. Sir Evelyn de Rothschild will step down as head of the London arm of the business after 21 years. “If you have four legs to a table, it's more stable than if you have two,” explained Baron David.

Vows of poverty are no obstacle to a keen commercial sense. The Missionaries of Charity, an order of nuns founded by **Mother Teresa**, who died in 1997, applied to India's patent office for copyright on her name to stop others using it and her logo. The Mother Teresa Institute of Management has already agreed to change its title.

Just the job

Unemployment in Germany hit 9.4% in June, leaving some 4.4m people out of work. American unemployment rose to 6.4%, its highest level for nine years.



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Fighting terrorism

Unjust, unwise, unAmerican

Jul 10th 2003
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America's plan to set up military commissions for the trials of terrorist suspects is a big mistake

Get article background

YOU are taken prisoner in Afghanistan, bound and gagged, flown to the other side of the world and then imprisoned for months in solitary confinement punctuated by interrogations during which you have no legal advice. Finally, you are told what is to be your fate: a trial before a panel of military officers. Your defence lawyer will also be a military officer, and anything you say to him can be recorded. Your trial might be held in secret. You might not be told all the evidence against you. You might be sentenced to death. If you are convicted, you can appeal, but only to yet another panel of military officers. Your ultimate right of appeal is not to a judge but to politicians who have already called everyone in the prison where you are held “killers” and the “worst of the worst”. Even if you are acquitted, or if your appeal against conviction succeeds, you might not go free. Instead you could be returned to your cell and held indefinitely as an “enemy combatant”.

Sad to say, that is America's latest innovation in its war against terrorism: justice by “military commission”. Over-reaction to the scourge of terrorism is nothing new, even in established democracies. The British “interned” Catholics in Northern Ireland without trial; Israel still bulldozes the homes of families of suicide bombers. Given the barbarism of September 11th, it is not surprising that America should demand retribution—particularly against people caught fighting for al-Qaeda in Afghanistan.

This newspaper firmly supported George Bush's battles against the Taliban and Saddam Hussein. We also believe that in some areas, such as domestic intelligence gathering (see article), his government should nudge the line between liberty and security towards the latter. But the military commissions the Bush administration has set up to try al-Qaeda suspects are still wrong—illiberal, unjust and likely to be counter-productive for the war against terrorism.

A question of integrity

The day before America's Independence Day celebrations last week, the Pentagon quietly announced that Mr Bush had identified six “enemy combatants” as eligible for trials before military commissions, which are to be set up outside America's civilian and military court systems. The Pentagon did not release the names of the accused, or any charges against them, but the families of two British prisoners and one Australian held at the American naval base at Cuba's Guantanamo Bay were told by their governments that their sons were among the six deemed eligible for trial.

The Australian government's failure to protest about this has caused protests (see article). British ministers have expressed “strong reservations” about the commissions. In the past, they have asked for British citizens caught in Afghanistan to be sent home for trial in British courts—just as Mr Bush allowed John Walker Lindh, a (white, middle-class Californian) member of the Taliban, to be tried in American courts.

American officials insist that the commissions will provide fair trials. The regulations published by the Pentagon stipulate that the accused will be considered innocent until proven guilty beyond a reasonable doubt, that he cannot be compelled to testify against himself, and that the trials should be open to the

press and public if possible.

The problem is that every procedural privilege the defendant is awarded in the regulations is provisional, a gift of the panel which is judging him. The regulations explicitly deny him any enforceable rights of the sort that criminal defendants won as long ago as the Middle Ages. Moreover, the planned commissions lack the one element indispensable to any genuinely fair proceeding—an independent judiciary, both for the trial itself and for any appeal against a conviction. The military officers sitting as judges belong to a single chain of command reporting to the secretary of defence and the president, who will designate any accused for trial before the commissions and will also hear any final appeals. For years, America has rightly condemned the use of similar military courts in other countries for denying due process.

Why dispense with such basic rules of justice? Mr Bush's officials say they must balance the demand for fair trials with the need to gather intelligence to fend off further terrorist attacks. Nobody denies that fighting terrorism puts justice systems under extraordinary strain. But this dilemma has frequently been faced by others without resorting to military trials. The established procedure is to pass special anti-terrorism laws, altering trial rules somewhat to handle terrorist cases, but not abandoning established court systems, and trying to retain the basic rights of those accused as far as possible. Britain and Spain have done this. There is no reason why America's own civilian courts, which have successfully tried plenty of domestic and foreign terrorists (including Mr Lindh), could not be adapted to this purpose.

Since the 2001 attacks, the Bush administration has avoided America's own courts repeatedly. Soon after the attacks, Mr Bush issued his executive order permitting military commissions outside the purview of the courts. Since then, his administration has imprisoned some 680 people at Guantanamo Bay precisely because it believed that the naval base, held on a perpetual lease, is outside the reach of anyone's courts, including America's. It has also claimed the right to arrest American citizens, even on American soil, as “enemy combatants” and to imprison them without charge until the war on terrorism is over. Appeals by civil libertarians to America's court system have been resisted at every stage.

Mr Bush could have asked Congress to pass new anti-terrorism laws. Instead, he is setting up a shadow court system outside the reach of either Congress or America's judiciary, and answerable only to himself. Such a system is the antithesis of the rule of law which the United States was founded to uphold. In a speech on July 4th, Mr Bush rightly noted that American ideals have been a beacon of hope to others around the world. In compromising those ideals in this matter, Mr Bush is not only dismaying America's friends but also blunting one of America's most powerful weapons against terrorism.

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Hong Kong and China

Rebellion

Jul 10th 2003
From The Economist print edition

Forcing a backdown over Hong Kong's new internal-security law could be only the beginning

Get article background

AFP

THE events of the past few days in Hong Kong have been not just the most momentous since Britain handed its colony back to China in 1997, but the most momentous for China itself since the Tiananmen Square demonstrations in 1989. In one way, perhaps, they may prove to be even more important. The students and workers whom the Chinese regime so bloodily suppressed failed to achieve any of their objectives, and the democracy movement they represented has since been extirpated with great ruthlessness. The 500,000 people who turned out on July 1st, to demonstrate against plans to impose an internal-security law on Hong Kong against the wishes of its people, have forced an official backdown. Ostensibly, this is merely a defeat for Hong Kong's government. But since Hong Kong's chief executive, the hapless Tung Chee-hwa, was appointed on China's say-so by a rubber-stamp electoral college, the real defeat is China's. Never before, in the 54-year history of the People's Republic, has peaceful popular protest achieved anything of the kind.

The bill the Hong Kong government had proposed to pass was a bad one. It did have a legal obligation to pass an internal-security bill of some kind, one laid upon it by Article 23 of the Basic Law, the mini-constitution that governs the Hong Kong Special Administrative Region and its relations with the central government in Beijing. But the Hong Kong government's proposed draft went well beyond the necessary minimum to meet that obligation.

For example, it proposed a legal basis for allowing the banning of political or indeed other groups simply for being subordinate to ones that had previously been proscribed in mainland China on national security grounds. Following howls of protests, a number of safeguards were built in. Yet the fear remained that the legislation might one day be used to ban the Falun Gong, an exercise group that is harmless in Hong Kong but which China loathes pathologically as a political threat on the mainland—or, perhaps, any Hong Kong pro-democracy group attempting to maintain links with China's underground democracy movement. Equally alarming were clauses that infringed on the rights of the press and extended the police's right of search.

Like a doomed balloonist throwing out ballast, in vain did Mr Tung attempt to ditch these controversial clauses following the July 1st demonstration. Yet his real problem is not just the internal-security bill, but the collapse of trust in the government that proposes to enforce it. The fact is that, under British rule, Hong Kong had any number of draconian statutes on its books. But the governor in Hong Kong was answerable to the government in London, and so to a democracy. Hong Kong's new laws would be administered by Mr Tung, a well-connected businessman originally from Shanghai, who has never been elected by anyone except a committee selected by China, and never could be. He thought he could get his bill through Hong Kong's parliament because only 24 of its 60 seats are directly elected—and a proportional-representation system in those elections further cuts the democrats down to size. In the end, though, the bill and the popular protests were too much even for some of Mr Tung's usually reliably pro-China allies to swallow, and they jumped clear (see article).

We, the people

The protesters are now demanding that, no matter what concessions may be offered, there should be no internal-security bill voted on until Hong Kong is a democracy, since only a democracy should be trusted with such powers. Having the whole of the legislature, and the chief executive to boot, elected by universal suffrage, is an option under the Basic Law, though not until 2007 at the earliest. One of Mr Tung's many failings is that he has refused even to open a discussion about what sort of electoral system Hong Kong should have, although the date of 2007 is starting to loom larger. And it is not just Mr Tung who is the problem: his “cabinet” is stuffed with people who would not sit comfortably in a proper democracy. The financial secretary, Anthony Leung, bought himself an expensive luxury car, shortly before announcing a tax hike on expensive luxury cars; Regina Ip, the much-disliked security secretary, ineptly dismissed the July 1st protesters as having nothing better to do on a public holiday.

But the demand for real accountability puts Hong Kong directly on a collision course with China, whose leaders, though they have never said it, surely hate the idea of full-blown democracy in any part of their domain. All this week and last, the censors in Beijing have been ripping photographs of the Hong Kong demonstrations out of newspapers and magazines, including last week's *Economist*.

It is too early to say whether plans for more direct elections in Hong Kong, or even just the spectacle of “people power” in action, will stir up demands for the same thing in China proper. By delivering economic development and greatly extended personal freedoms, the Communists on the mainland have bought themselves time. But what happens in Hong Kong, now that it is fully part of China, is bound to have an impact. Back in 1997, we and others expressed the hope that, in time, Hong Kong might act as a catalyst for political change in China. This could still happen.

In the meantime, however, China and Mr Tung have some difficult decisions to make. Should he resign? It is hard to imagine China being prepared to accept the loss of face this would involve, though a little pain now might avoid a lot more later—as China may already be realising, having missed an opportunity to dump Mr Tung quietly when he was up for re-appointment last year. And what should happen to the internal-security bill? Boneheadly, one Chinese government legislator demanded last week that the passage of the bill should go ahead as planned, oblivious to political reality.

For now, there is little chance of getting any sort of bill through the Legislative Council—which on July 9th was again surrounded by tens of thousands of protesters. A lengthy, preferably indefinite, period of consultation and committee-work is likely. To pick a fight would be to risk losing it.

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Mexico's congressional election

Wounded and at bay

Jul 10th 2003
From The Economist print edition

Ways for Vicente Fox to break Mexico's dangerous political deadlock

AP

Get article background

THREE years ago, in a historic election, Vicente Fox ended seven decades of rule by Mexico's Institutional Revolutionary Party (PRI). Mr Fox, a former manager at Coca-Cola, swept into the presidency promising to turn his country into a full democracy, and many other sweet things besides. But reality has proved sour. The economy is stagnant, and most of the promised changes have been blocked by a hostile legislature.

Much was therefore at stake in last Sunday's mid-term election, for the 500-seat lower house of Congress. Victory for Mr Fox's conservative National Action Party (PAN) would have allowed the president to push his reforms boldly forward. But the voters had other ideas. The outcome was an unexpectedly heavy defeat for the PAN and for the government (see article). The PRI, which three years ago was widely expected to splinter into irrelevance, emerged fewer than 30 seats short of a majority. The leftish Party of the Democratic Revolution almost doubled its seats.

In fact, the election was hardly an endorsement of the opposition. Mr Fox himself remains popular, but his government is not. The PAN suffered mainly because many of those who voted for Mr Fox as president stayed away this time.

It is not the president's fault that he took office just as the American economy slowed to a crawl, halting growth in Mexico. But that makes his reforms all the more vital: for Mexico to grow, its businesses need to be far more competitive, and that means allowing private investment in energy, reforming the labour market and rationalising taxes. Unfortunately, the prospects for all that now look even bleaker. Mexico faces another three years of policy drift and legislative gridlock.

What can the president do to make the best of this bad job? He could start with more efforts to cut deals with the PRI. Mr Fox has so far been a poor negotiator and tactician, and few of his ministers have been any better. Optimists reckon that the main opposition parties, each of which now nourishes hope of winning the presidency in 2006, will have an interest in backing limited reforms, to ensure that Mexico remains governable. If so, Mr Fox needs to take advantage of that.

A more tangible crumb of comfort is that under Mr Fox, Mexico has at least been economically and financially stable. Provided his government sticks to its prudent macroeconomic policies, growth will eventually pick up, as and when the American economy moves into higher gear.

But Mr Fox's best chance of going down in Mexican history as something other than a big disappointment may be to go for political and institutional reforms. Not only would these tackle the legacies of authoritarianism, but some of them might have a decent chance of approval. One such measure would be to repeal the ban on legislators serving for more than one term; the rule ensures that congressmen lack experience, and it makes them less accountable to voters.

A still bolder step would be to shorten the presidential term, but to permit a second one. A single six-year term for an all-powerful president suited the old Mexico. But one-party rule has given way to a three-party system (plus some smaller outfits), and voters deserve wider and more frequent choice. Boldest of all would be to adopt parliamentary government. That is doubtless too radical for a country

that has been in thrall to omnipotent leaders since the Aztecs. But fresh thought is urgently needed if Mexico's political deadlock is not to endanger its future stability.

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Asian currencies

Re-orientation needed

Jul 10th 2003
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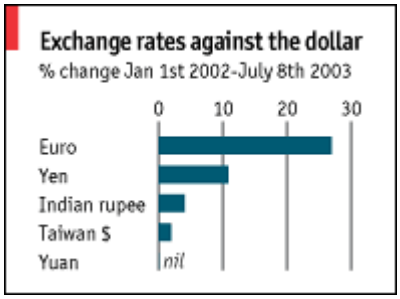
Asian countries' efforts to hold down their currencies are misguided



DOES somebody in your office not pull their weight, loading the hardest jobs on to others? This breeds resentment—and so it can at the global level. Today's beef is that the burden of the dollar's decline is not being fairly shared. The dollar has fallen by around a quarter against the euro since early 2002; yet it is unchanged against the Chinese yuan, which has a dollar peg, and barely down against other Asian currencies. Asia's shirkers should now let their currencies rise too.

To argue that China ought to revalue does not mean accepting some popular claims, notably that it is to blame for America's huge trade deficit and for exporting deflationary pressures. These claims are nonsense. Imports from China amount to less than 2% of GDP in America and Japan, so they cannot cause deflation. And America's trade deficit is the result of years of excessive consumer spending. It is, however, true that the Chinese yuan and other regional currencies are being deliberately held down. And, at a time when the dollar is falling and America needs to narrow its current-account deficit, Asia's currency rigidity is increasing strains on the world economy. In particular, the euro is having to rise by more than it should, pushing it towards dangerously overvalued levels.

As the dollar has swooned, Asian central banks have been intervening massively to hold down their currencies. As a result, official coffers are bulging with foreign-currency reserves (see article). Mercantilist governments may see this as a sign of strength. In fact excess reserves can point to poor economic management. Reserves are often invested in low-yielding Treasury bills—which is like a firm leaving cash idle in the bank rather than putting it to productive use or returning it to shareholders. Asian countries would benefit if the money were instead invested at home or used to boost consumer spending.

Cheap currencies boost exports, but discourage domestic spending by making imports dearer. Asian economies are more dependent on exports than ever. After the Asian crisis in 1997, super-competitive currencies helped exports to boom, but domestic demand has lagged. So exports now account for an average of 64% of the region's GDP, up from 55% in the early 1990s. Governments fret that stronger currencies would make exports less competitive, but they would also encourage firms to shift upmarket from low-skilled to higher-skilled labour, which is essential for long-term prosperity. Allowing currencies to rise is therefore in many countries' own best interests. There is, admittedly, a specific problem with China: freely floating the yuan would be risky so long as Chinese banks are laden with bad debts and the financial system is fragile. But it would be perfectly possible to re-peg the yuan at a higher parity, keeping capital controls for the time being.

Stronger Asian currencies would take the pressure off the euro and help America's trade deficit to shrink. America's government has urged China and other Asians to stop intervening. Yet, ironically, Asia's massive accumulation of reserves is helping to prop up the American economy. By buying Treasury and government-agency debt, central banks have financed America's current-account deficit, and pushed down bond yields and mortgage rates, allowing America's consumer spending and borrowing binge to continue for longer. This has enabled households to postpone their post-bubble belt-tightening. But because consumer debt and the current-account deficit have swelled further, it means that the eventual adjustment, when it comes, will be more painful.

Perhaps the biggest reason why China and its neighbours should not keep their cheap currencies is that they will stoke protectionist sentiment abroad. As one of the main beneficiaries of freer trade, Asia would be a big loser from that.

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WMD and Iraq

Artificial intelligence?

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From The Economist print edition

Britain needs a judicial inquiry to find out what went wrong with intelligence on Iraq

Reuters

THE row over the British government's use of intelligence in the run-up to the war in Iraq has served those involved rather well. The government, which the BBC had accused of “sexing up” intelligence for publication to strengthen the case for war, was cleared on most charges by a report published on July 7th by the House of Commons foreign affairs select committee. The BBC, which the Tory party often accuses of being the government's patsy, has had a fine opportunity to prove its independence from Downing Street. The committee members, backbenchers unaccustomed to the limelight, got their moment of fame. The only people who have so far done badly out of the affair are the voters, who are not much wiser than they were before this row started a month ago about why it is that Britain went to war to avert an apparent threat for which little fresh evidence has yet been found.

The select committee's report goes some way towards answering the narrow questions which have preoccupied British pundits and politicians for the past month. Did Alastair Campbell, Tony Blair's chief spin-doctor, insert in a late draft of an intelligence dossier published in September the claim that Saddam Hussein had weapons of mass destruction that could be launched within 45 minutes? According to a majority of the committee, the evidence available suggests that he did not. Did Tony Blair mislead Parliament about the provenance of a dossier published in February, which he claimed was “intelligence” but which turned out, in part, to come from an old PhD thesis? He did, according to the committee, though not knowingly. But the report does not answer a more important, and wider, question: why did the government believe that Iraq posed a substantial threat at all? A second report, this one from the intelligence services committee (ISC), is due before Parliament rises in ten days' time, but there is little chance that it will produce a satisfactory answer. It is made up of members hand-picked by the prime minister who have a cosy relationship with the spies.

Parliamentary committees have neither the powers nor the resources to conduct thorough investigations: the Commons foreign affairs committee has six staff compared with the Senate foreign affairs committee's 44. Each MP on the committee has a secretary and researcher (if he is lucky) compared with each senator's 30-odd staff. British committees cannot compel ministers to give evidence, for the government can put the matter to a vote in the house, which the government will win. The dissenting minority on the foreign affairs committee complained of being denied important documents. The ISC's reports go to the prime minister before they are published, for him to strike out whatever he likes.

The check's in the post

The reason for the parliamentary committees' feebleness goes back to the flawed way in which Britain is run. America has a constitution which sets up its legislature—including its powerful congressional committees—as a check on the executive. Britain has no constitution and a Parliament whose clout is limited by the power of prime ministerial patronage and MPs' dependence on their party machines. The foreign affairs committee offered a fine illustration of this. It divided on party lines. Labour members said the government behaved fairly well. Tories and Lib Dems said it may not have. Astonishing.

Parliamentary committees don't have the credibility, the power or the resources to get to the bottom of what went on between the government and the intelligence services in the run-up to the war. An

independent judicial inquiry, with the power to summon anybody it likes and to take evidence in private as well as in public, might. If Tony Blair wants to prove he has nothing to be ashamed of, he should set one up.

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Letters

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From Economist.com

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Dean's appeal

SIR – Lexington suggests that Howard Dean is unelectable because his views are too radical (June 28th). It is the Bush agenda that is extremist. As governor of Vermont, Mr Dean balanced the budget, supported civil rights, protected the environment and was indeed "a pragmatic New Democrat in the Clinton mould."

In contrast, George Bush has pushed a reckless financial policy, turned an inherited surplus to record deficits and undercut the financial base of what the federal government has guaranteed to Americans for decades to come. The Bush team has replaced historic alliances and international treaties with unilateralist arrogance, started a pre-emptive war based on shaky intelligence, reversed environmental protection and squandered worldwide sympathy for September 11th and the goodwill earned by generations of Americans. Mr Dean stands in the line of traditional values of western democracies; the current administration does not.

Stephen Reynes
Calais, Vermont

SIR – Let's see? Mr Dean is for the death penalty, against gun control, for fiscal responsibility and wary of foreign entanglements. How do you define conservative?

Geoff Berg
Warren, Rhode Island

SIR – Comparing Mr Dean to Walter Mondale is ludicrous. Mr Mondale was no insurgent but rather a classic, boring, inside-the-Beltway, establishment candidate—like John Kerry, Joe Lieberman, Dick Gephardt or even Al Gore. The real Democratic insurgent in 1984 was Gary Hart. He ran to the right of Mr Mondale in the primaries, appealed strongly to independents and would have given Ronald Reagan a much tougher race. Mr Dean appeals to many of the same angry centrists who supported Mr Hart in 1984, Ross Perot in 1992 and John McCain in 2000. As a successful (though initially little-known) governor, Mr Dean looks an awful lot like Jimmy Carter or Bill Clinton, the only Democrats to win the White House in the past 35 years.

Bryan Wildenthal
San Diego

SIR – You say that President William McKinley "was able to usher in 30 years of Republican hegemony". In fact, Republicans controlled the White House for only 16 years until Woodrow Wilson took over for two terms. For nearly half that time, Theodore Roosevelt was president.

Joseph Curro
Arlington, Massachusetts

Cosmetic difference

SIR – You say that "Estée Lauder and Revlon are more dependent on unfashionable department stores where sales are declining and selling costs are high" ("Pots of promise", May 24th). Revlon's trade is that

of mass retail distribution in North America and not department stores. This is an important distinction as mass colour cosmetics are a growing category for us, as you clearly state.

Catherine Fisher
Corporate communications
Revlon
New York

Tar very much

SIR – Canada's oil sands are a world-scale resource ("There's oil in them thar sands!", June 28th). Not only are there billions of barrels of oil in the ground that require no further exploration expenditures and can be produced without decline for decades, they are in a stable country, adjacent to the largest market in the world. Shell Canada's Athabasca Oil Sands Project recently commenced operations. It is true that development costs of this resource are higher than the conventional output of the big OPEC producers. However, our target production cost of C$12 ($9) a barrel means that production could survive a dramatic price collapse like the world saw five years ago.

Tim Faithfull
President and CEO
Shell Canada
Calgary

All work and no play?

SIR – Studies of cabbies, bicycle messengers and stadium food-vendors are used to support the conclusion that "higher returns encourage more effort, not more leisure, when people have some control over their work hours" (Economics focus, June 28th). The studies merely show that these workers will increase their hours when returns are temporarily higher rather than choosing more leisure immediately. They do not show a long-run effect. Moreover, most tax cuts for people in lower tax brackets are small, unlike the substantial rises in incomes seen in those studies.

Richard Greene
Princeton, New Jersey

SIR – What happens to the economy when the tax cuts for the rich "trickle down" to increase property taxes on homes, small business and farmers or sales taxes go up to pay for essential services including education?

Carman Hill
Ithaca, New York

The magic's gone

SIR – Your article on the world economy concludes that: "Even [Alan] Greenspan's wizardry may not be enough to ensure a sustained healthy recovery" ("Breaking the deflationary spell", June 28th). But consider his record of wizardry: in 1974, when he was in charge of the Council of Economic Advisers, inflation got out of control; in 1987, as the newly appointed chairman of the Federal Reserve, Mr Greenspan presided over America's biggest-ever one-day stockmarket downturn; in 1998, he bailed-out Long-Term Capital Management (along with its greedy investors); in 1999, he panicked and printed more money, rather than gradually deflating the bubble; in 2001, he panicked again and printed more money. Of late, his wizardry has amounted to driving down interest rates, resulting in the current housing and consumption bubble.

Wall Street as well as a few financial publications would do themselves well to consider what kind of wizard Mr Greenspan really is.

Christopher Yeanos
Washington, DC

Rounded education

SIR – The argument that some individuals should forgo a university education assumes that its only measure of value is the increased earnings a graduate stands to make ("Money back", June 21st). Other benefits of attending university, such as improved critical thinking and acquiring a lifelong love for learning, while less tangible, clearly provide enormous value to the individual and society. We should be more concerned about the growing perception that university is simply a means to a larger salary. This threatens the basic principles upon which these institutions were founded.

Brandon Duncan
San Jose, California

Flagging interest

SIR – The home with a flag-draped front porch that illustrates your article on Fannie Mae and Freddie Mac could probably say "No thanks" to the two institutions ("Crony capitalism", June 28th). A count of 43 stars indicates that this is the official flag of the United States for the year 1890, way preceding Fannie and Freddie.

David Conell
Albuquerque, New Mexico

A question of intelligence

SIR – In your extensive reporting on the Iraq-Niger uranium scandal ("Not very intelligent", Economist.com, July 9th), one struggles to find the answer to three very basic questions: Who forged the documents? Why? And how did the British and American intelligence services obtain them? Perhaps one of your more enterprising reporters could tell us.

K. Weisbrode
Cambridge, Massachusetts

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150 years after Commodore Perry

Japanese spirit, western things

Jul 10th 2003 | TOKYO
From The Economist print edition

Bridgeman

Learning the wrong lessons

When America's black ships forced open Japan, nobody could have predicted that the two nations would become the world's great economic powers

OPEN up. With that simple demand, Commodore Matthew Perry steamed into Japan's Edo (now Tokyo) Bay with his “black ships of evil mien” 150 years ago this week. Before the black ships arrived on July 8th 1853, the Tokugawa shoguns had run Japan for 250 years as a reclusive feudal state. Carrying a letter from America's president, Millard Fillmore, and punctuating his message with cannon fire, Commodore Perry ordered Japan's rulers to drop their barriers and open the country to trade. Over the next century and a half, Japan emerged as one of history's great economic success stories. It is now the largest creditor to the world that it previously shunned.

Attempts to dissect this economic “miracle” often focus intently on the aftermath of the second world war. Japan's occupation by the Americans, who set out to rebuild the country as a pacifist liberal democracy, helped to set the stage for four decades of jaw-dropping growth.

Yet the origins of the miracle—and of the continual tensions it has created inside Japan and out—stretch further back. When General Douglas MacArthur accepted Japan's surrender in 1945 aboard the battleship *Missouri*, the Americans made sure to hang Commodore Perry's flag from 1853 over the ship's rear turret. They had not only ended a brutal war and avenged the attack on Pearl Harbour—they had also, they thought, won an argument with Japan that was by then nearly a century old.

America's enduring frustration—in the decades after 1853, in 1945, and even today—has not been so much that Japan is closed, but that it long ago mastered the art of opening up on its own terms. Before and after those black ships steamed into Edo Bay, after all, plenty of other countries were opened to trade by western cannon. What set Japan apart—perhaps aided by America's lack of colonial ambition—was its ability to decide for itself how to make the process of opening suit its own aims.

One consequence of this is that Japan's trading partners, especially America, have never tired of complaining about its economic practices. Japan-bashing reached its most recent peak in the 1980s, when American politicians and businessmen blamed “unfair” competition for Japan's large trade surpluses. But similar complaints could be heard within a few decades of Commodore Perry's mission. The attitude was summed up by “Mr Dooley”, a character created by Peter Finley Dunne, an American

satirist, at the close of the 19th century: “Th' trouble is whin the gallant Commodore kicked opn th' door, we didn't go in. They come out.”

Nowadays, although poor countries still want Japan (along with America and the European Union) to free up trade in farm goods, most rich-country complaints about Japan are aimed at its approach to macroeconomics and finance, rather than its trade policies. Japan's insistence on protecting bad banks and worthless companies, say its many critics, and its reluctance to let foreign investors help fix the economy, have prevented Japanese demand from recovering for far too long. Once again, the refrain goes, Japan is unfairly taking what it can get from the world economy—exports and overseas profits have been its only source of comfort for years—without giving anything back.

While these complaints have always had some merit, they have all too often been made in a way that misses a crucial point: Japan's economic miracle, though at times paired with policies ranging from protectionist to xenophobic, has nevertheless proved a huge blessing to the rest of the world as well. The “structural impediments” that shut out imports in the 1980s did indeed keep Japanese consumers and foreign exporters from enjoying some of the fruits of that miracle; but its export prowess allowed western consumers to enjoy better and cheaper cars and electronics even as Japanese households grew richer.

Similarly, Japan's resistance to inward investment is indefensible, not least because it allows salvageable Japanese companies to wither; but its outward investment has helped to transform much of East Asia into a thriving economic region, putting a huge dent in global poverty. Indeed, one of the most impressive aspects of Japan's economic miracle is that, even while reaping only half the potential gains from free trade and investment, it has still managed to do the world so much good over the past half-century.

Setting an example

Arguably, however, Japan's other big effect on the world has been even more important. It has shown clearly that you do not have to embrace “western” culture in order to modernise your economy and prosper. From the very beginning, Japan set out to have one without the other, an approach encapsulated by the saying “Japanese spirit, western things”.

How did Japan pull it off? In part, because the historical combination of having once been wide open, and then rapidly slamming shut, taught Japan how to control the aperture through which new ideas and practices streamed in. After eagerly absorbing Chinese culture, philosophy, writing and technology for roughly a millennium, Japan followed this with 250 years of near-total isolation. Christianity was outlawed, and overseas travel was punishable by death.

Although some Japanese scholars were aware of developments in Europe—which went under the broad heading of “Dutch studies”—the shoguns strictly limited their ability to put any of that knowledge to use. They confined all economic and other exchanges with Europeans to a tiny man-made island in the south-western port of Nagasaki. When the Americans arrived in 1853, the Japanese told them to go to Nagasaki and obey the rules. Commodore Perry refused, and Japan concluded that the only way to “expel the barbarians” in future would be to embrace their technology and grow stronger.

AP

Learning the wrong lessons

But once the door was ajar, the Japanese appetite for “western things” grew unbounded. A modern guidebook entry on the port city of Yokohama, near Tokyo, notes that within two decades of the black ships' arrival it boasted the country's first bakery (1860), photo shop (1862), telephone (1869), beer brewery (1869), cinema (1870), daily newspaper (1870), and public lavatory (1871).

Yet, at the same time, Japan's rulers also managed to frustrate many of the westerners' wishes. The constant tension between Japan's desire to measure up to the West—economically, diplomatically, socially and, until 1945, militarily—and its resistance to cultural change has played out in countless ways, good and bad, to this day.

Much of it has reflected a healthy wish to hang on to local traditions. This is far more than just a matter of bowing and sleeping on futons and tatami, or of old women continuing to wear kimonos. The Japanese have also clung to distinct ways of speaking, interacting in the workplace, and showing each other respect, all of which have helped people to maintain harmony in many aspects of everyday life.

Unfortunately, however, ever since they first opened to the West, anti-liberal Japanese leaders have preferred another interpretation of “Japanese spirit, western things”. Instead of simply trying to preserve small cultural traditions, Japan's power-brokers tried to absorb western technology in a way that would shield them from political competition and protect their interests. Imitators still abound in Japan and elsewhere.

In East Asia alone, Malaysia's Mahathir Mohamad, Thailand's Thaksin Shinawatra, and even the Chinese Communist Party all see Japan as proof that there is a way to join the rich-country club without making national leaders or their friends accountable. These disciples of Japan's brand of modernisation often use talk of local culture to resist economic and political threats to their power. But they are careful to find ways to do this without undermining all trade and investment, since growth is the only thing propping them up.

Japan's first attempt to pursue this strategy, it must never be forgotten, grew increasingly horrific as its inconsistencies mounted. In 1868, while western writers were admiring those bakeries and cinemas, Japan's nationalist leaders were “restoring” the emperor's significance to that of an imaginary golden age. The trouble, as Ian Buruma describes in his new book, “Inventing Japan” (see article), is that the “Japanese spirit” they valued was a concoction that mixed in several bad western ideas: German theories on racial purity, European excuses for colonialism, and the observation from Christianity that a single overarching deity (in Japan's case the newly restored emperor) could motivate soldiers better than a loose contingent of Shinto gods. This combination would eventually whip countless young Japanese into a murderous xenophobic frenzy and foster rapacious colonial aggression.

It also led Japan into a head-on collision with the United States, since colonialism directly contradicted America's reasons for sending Commodore Perry. In “The Clash”, a 1998 book on the history of American-Japanese relations, Walter LaFeber argues that America's main goal in opening Japan was not so much to trade bilaterally, as to enlist Japan's support in creating a global marketplace including, in particular, China.

At first, the United States opened Japan because it was on the way to China and had coal for American steamships. Later, as Japan gained industrial and military might, America sought to use it as a counterweight to European colonial powers that wanted to divide China among their empires. America grew steadily more furious, therefore, as Japan turned to colonialism and tried to carve up China on its own. The irony for America was that at its very moment of triumph, after nearly a century of struggling with European powers and then Japan to keep China united and open, it ended up losing it to communism.

A half-century later, however, and with a great deal of help from Japan, America has achieved almost exactly what it set out to do as a brash young power in the 1850s, when it had barely tamed its own continent and was less than a decade away from civil war. Mainland China is whole. It has joined the World Trade Organisation and is rapidly integrating itself into the global economy. It is part of a vast East Asian trade network that nevertheless carries out more than half of its trade outside the region. And this is all backed up by an array of American security guarantees in the Pacific. The resemblance to what America set out to do in 1853 is striking.

For both Japan and America, therefore, the difficult 150-year relationship has brought impressive results.

They are now the world's two biggest economies, and have driven most of the world's technological advances over the past half-century. America has helped Japan by opening it up, destroying its militarists and rebuilding the country afterwards, and, for the last 50 years, providing security and market access while Japan became an advanced export dynamo. Japan has helped America by improving on many of its technologies, teaching it new manufacturing techniques, spurring on American firms with its competition, and venturing into East Asia to trade and invest.

And now?

What, then, will the continuing tension between Japanese spirit and western things bring in the decades ahead?

For America, though it will no doubt keep complaining, Japan's resistance to change is not the real worry. Instead, the same two Asian challenges that America has taken on ever since Commodore Perry sailed in will remain the most worrying risks: potential rivalries, and the desire by some leaders to form exclusive regional economic blocks. America still needs Japan, its chief Asian ally, to combat these dangers. Japan's failure to reform, however, could slowly sap its usefulness.

For Japan, the challenges are far more daunting. Many of them stem from the increasing toll that Japan's old ways are taking on the economy. Chief among these is Japan's hostility towards competition in many aspects of economic life. Although competitive private firms have driven much of its innovation and growth, especially in export-intensive industries, Japan's political system continues to hobble competition and private enterprise in many domestic sectors.

AP

If at first you don't succeed

In farming, health care and education, for example, recent efforts to allow private companies a role have been swatted down by co-operatives, workers, politicians and civil servants. In other inefficient sectors, such as construction and distribution, would-be losers continue to be propped up by government policy. Now that Japan is no longer growing rapidly, it is harder for competitive forces to function without allowing some of those losers to fail.

Japan's foreign critics are correct, moreover, that its macroeconomic and financial policies are a disgrace. The central bank, the finance ministry, the bank regulators, the prime minister and the ruling-party politicians all blame each other for failing to deal with the problems. All the while, Japan continues to limp along, growing far below its potential as its liabilities mount. Its public-sector debt, for instance, is a terrifying 140% of GDP.

Lately, there has been much talk about employing more western things to help lift Japan out of its mess. The prime minister, Junichiro Koizumi, talks about deregulatory measures that have been tried in North America, Europe and elsewhere. Western auditing and corporate governance techniques—applied in a Japanese way, of course—are also lauded as potential fixes. Even inward foreign direct investment is held out by Mr Koizumi as part of the solution: he has pledged to double it over the next five years.

The trouble with all of these ideas, however, is that nobody in Japan is accountable for implementing them. Moreover, most of the politicians and bureaucrats who prevent competitive pressures from driving change are themselves protected from political competition. It is undeniable that real change in Japan

would bring unwelcome pain for many workers and small-business owners.

Still, Japan's leaders continue to use these cultural excuses, as they have for 150 years, to mask their own efforts to cling to power and prestige. The ugly, undemocratic and illiberal aspects of Japanese traditionalism continue to lurk behind its admirable elements.

One reason they can do so is because Japan's nationalists have succeeded completely in one of their original goals: financial independence. The desire to avoid relying on foreign capital has underlain Japan's economic policies from the time it opened up to trade. Those policies have worked. More than 90% of government bonds are in the hands of domestic investors, and savings accounts run by the postal service play a huge role in propping up the system.

Paradoxically, financial self-reliance has thus become Japan's curse. There are worse curses to have, of course: compare Japan with the countless countries that have wrecked their economies by overexposing themselves to volatile international capital markets. Nevertheless, Japan's financial insularity further protects its politicians, who do not have to compete with other countries to get funding.

Theories abound as to how all of this might change. Its history ought to remind anyone that, however long it takes, Japan usually moves rapidly once a consensus takes shape. Potential pressures for change could come from the reversal of its trade surpluses, an erosion of support from all those placid postal savers, or the unwinding of ties that allow bad banks and bad companies to protect each other from investors. The current political stalemate could also give way to a coherent plan, either because one political or bureaucratic faction defeats the others or because a strong leader emerges who can force them to co-operate.

The past 150 years suggest, however, that one important question is impossible to answer in advance: will it be liberalism or its enemies who turn such changes to their advantage? Too often, Japan's conservative and nationalist leaders have managed to spot the forces of change more quickly than their liberal domestic counterparts, and have used those changes to seize the advantage and preserve their power. Just as in the past, East Asia's fortunes still greatly depend on the outcome of the struggle between these perennial Japanese contenders.

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Foreign policy and domestic politics

And it used to be such a pleasure

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Support for the Bush administration's foreign policy may be starting to wobble. But can the Democrats take advantage?

HERE is something that doesn't happen every day: the Bush administration admitting it was wrong. In this case, that the president should not have claimed—as he did in his state-of-the-union address in January—that Iraq tried to buy yellow-cake uranium from Niger in an attempt to restart its nuclear-weapons programme.

Although a row has already broken out between the CIA and their British peers about who said what about Niger (see article), it would be wrong to make too much of this. The claim was only part of the allies' assertion that Iraq had weapons of mass destruction—and is arguably less significant than the discovery, in late June, of a centrifuge hidden 12 years ago in a scientist's backyard in Baghdad. That constituted the first piece of hard evidence that Iraq may indeed have been trying to retain some sort of nuclear capacity.

Still, this was also the first time the administration has retracted any of its arguments for overthrowing Saddam Hussein, or indeed admitted that it may have exaggerated the imminence of the Iraqi threat. And, along with other straws in the wind, it points to a possible new political problem for Mr Bush: public scepticism of America's foreign policy.

For almost two years, it has seemed a safe bet that, whatever else happened in American politics, George Bush had strong public support for his foreign policy, and that national security would be a big plus for him in the 2004 presidential election. Not only could he go on the hustings and proclaim victory in two wars but, more important, national security would remind voters of the quality which they say they most admire in him: leadership. More people attribute their liking of Mr Bush to this than to any particular achievement.

Yet in the past few weeks, the assumption that foreign policy must be good for Mr Bush has started to be tested. That is not to say that foreign affairs has become a political liability. Still, for the first time, the dangers of relying too heavily on security as a vote winner are becoming apparent. Whether Democrats are able to capitalise on this is a different question.

Bringing on trouble

The event that crystallised the change was Mr Bush's reaction to attacks against American soldiers in Iraq two weeks ago. “There are some who feel the conditions are such that they can attack us there,” he told a press conference on July 2nd. “My answer is: bring them on.”

This braggadocio prompted a furious and, for once, concerted response from Democrats. “The president who sent [American troops] on this mission showed tremendous insensitivity to the danger they face,” fumed Howard Dean, the former governor of Vermont. “The deteriorating situation in Iraq requires less swagger and more thoughtfulness,” said John Kerry, Mr Dean's arch-rival.

Actually, the swagger itself will not do Mr Bush much harm. Most voters like his lapses into bar-room bragging (he also said he wanted Osama bin Laden “dead or alive”). His job ratings remain high, though inching down. Mr Bush's spokesman claimed the president was merely expressing confidence in the army's ability to control Iraq. Other supporters argued he was sending a perfectly justified message to opponents of the Anglo-American occupation: we will not be pushed out, nor deflected from rebuilding the country.

Nevertheless, the spat over the president's remarks matters because the drip-drip of casualties and the endless problems of reconstruction seem to be having an impact. Since the end of major combat operations in May, 67 Americans have been killed in Iraq—almost half the number killed during the war itself (139). Twenty soldiers were injured the day after Mr Bush's “bring them on” comment.

As a result, support for the occupation is eroding. In mid-April, just after the fall of Baghdad, 73% of Americans said it was worth going to war in Iraq, according to a Gallup poll. The figure is now 56%. According to a Pew poll, the share of respondents who think the military effort is going very well has fallen by two-thirds, to just 23%.

As Jim Hoagland recently pointed out in the *Washington Post*, at this stage in the electoral cycle administrations usually start trying to minimise their exposure to foreign-policy risks. Like markets, politicians seeking re-election hate uncertainty—and foreign policy is inherently unreliable. Yet Mr Bush is doing the opposite.

In Iraq, he is reluctant to spread the risk by inviting in too many NATO or UN peacekeepers. This week, Donald Rumsfeld admitted that the cost of keeping America's 145,000 troops in Iraq was $3.9 billion a month (double the previous estimate). Peacekeepers may also be sent to Liberia.

This is risky because voters—and to some extent Mr Bush's generals—already think America is doing too much. In a recent study by the Programme on International Policy Attitudes, 62% said they think America plays the role of world policeman more than it should; two-thirds want American troops out of Saudi Arabia once Iraq is stabilised. At his farewell speech, the retiring army chief of staff, Eric Shinseki, said America was trying to carry out a 12-division strategy with a ten-division army. In other words, fears of overstretch are growing. America's traditionally reluctant internationalism seems at odds with Mr Bush's foreign assertiveness.

At the moment that friction is not so great as to limit the president's freedom of manoeuvre. But it does offer an opportunity to the Democrats. If they can articulate a plausible alternative, they should find a receptive public. At the moment, there is little sign of that happening.

Some of their presidential applicants have criticised policy in Iraq unapologetically, notably Mr Dean. But he says he would support sending peacekeepers to Liberia. Others (such as Senator Joe Lieberman) have backed Mr Bush over Iraq, with reservations. Still others have tried to do both at the same time. Senator Kerry voted for the resolution to send troops to Iraq, but he has complained about the president tricking the nation into war.

Of course, by next year the Democrats will have one presidential candidate and, presumably, one foreign-policy voice. That may make a difference. Until then, though, the American public is likely to remain what it has become in the past month: increasingly anxious about Iraq, and possible overstretch—but with no clear alternative to Mr Bush.

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Telling it to Iran

Prodding the clerics

Jul 10th 2003 | LOS ANGELES
From The Economist print edition

How southern California has become a centre of Iran's democratic opposition

AP

LA woman, Tehran song

EBI DAVOUDI scrolls through the e-mail and voice-mail messages to Radio Sedaye: 4,000 in the past ten days. He clicks on one. “My name is Puria,” it reads. “I am 19 years old, from Isfahan, and I agree with the petition to stop Iran being an Islamic republic.” In the studio next door, Saeed Ghaem-Maghami chairs a discussion about whether Iran needs socialism instead.

Beverly Hills and the San Fernando Valley may seem a long way from Tehran. But from southern California, Farsi-language broadcasts flow into Iran by satellite, the internet and short-wave radio. Between them, a dozen television and radio stations are covering Iran's politics 24 hours a day. Radio Sedaye is the oldest.

The United States has long provided a haven for opponents of other countries' governments. One of them, Sun Yat-Sen, who a century ago led the fight for a more democratic China, once stayed in Los Angeles's Chinatown, not far from where the Iranian stations are now broadcasting. Southern California is today home to around 1m Iranian-Americans. Most of the stations got their start broadcasting in Farsi to this domestic audience. And they still earn what money they have from local advertising.

Recent student demonstrations in Iran—a particularly emotional one was planned for this week but the security services kept it from getting out of hand—have given the stations new vigour. Although Iran's government disrupts satellite connections, so that it is hard to know exactly how many people tune in, they have a huge potential audience. They also have a compelling subject, showing the demonstrations and running uncensored call-in programmes. They have become part of Iran's politics. In May both the country's clerical boss, Ayatollah Ali Khamenei, and its more liberal-minded president, Muhammad Khatami, accused the students' leaders of “collaborating with Iran's enemies”.

Some stations welcome the controversy. They broadcast the place and time of demonstrations, and call on listeners to join in. They argue that the job of a free press includes helping to overthrow autocratic regimes. Others are more cautious, arguing that broadcasters should keep their distance from specific political ideas—and from America.

This matters, because Senator Sam Brownback of Kansas is sponsoring an Iran Democracy Act that, if passed, would give $50m to the Iranian opposition, some of it for Los Angeles-based broadcasters. Would this help the regime's opponents by encouraging more anti-government broadcasting, or hamper them by making the programmes seem like American propaganda? Both, maybe.

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About sponsorship

Not enough houses in California

Homeless masses

Jul 10th 2003 | LOS ANGELES
From The Economist print edition

Housing may be California's biggest long-term problem

“CHAVEZ RAVINE”, a theatrical hit in Los Angeles, has an odd subject: building a baseball stadium on a former shanty town. Musical satire about housing is not exactly common. But this has struck a chord. House prices may be soaring and sprawl remains a common complaint, but the polls still show most Californians want more housing to be built.

Houses are as much part of the Californian dream as jobs. The state has long offered waves of migrants, from dust-bowl refugees to Mexicans, a place to work and live. In Los Angeles, this has produced a 100-mile-wide city.

Yet California has stopped building enough houses. The rule of thumb is that you need one new house for every 1.5 new jobs. In 2002, the rate was only one new house for 3.5 jobs. In the biggest cities, such as Los Angeles, it is more like one to five. Over the past decade, California has drawn in 11m new immigrants, but built only 1.3m new houses. By most estimates that is 1m short of what is needed. Even if the state were to stop attracting (or breeding) people, it would take seven years, at current building rates, to end the backlog.

Predictably, strong demand and weak supply have pushed prices to record levels. Median house prices in California rose by 16% in the year to May, to $369,000. In America, 65% of people on average incomes can afford a median-price house. In California, the share is 27%, down from 40% in the mid-1990s; 16 of the top 20 “least affordable” housing markets in the country are in California.

In northern California, the middle classes are worried about a housing bubble. This week, figures released by the Census Bureau showed that the hitherto fast-growing cities around Silicon Valley, including San Francisco, have started to lose population in the wake of the dotcom bust. But house prices are still rising—partly because people have been investing in property rather than high-tech shares.

In southern California, the poor are worried about finding anywhere to live. In east Los Angeles, a Mexican-dominated part of the city, there is an average of 2.5 households in each housing unit. A third of Latino households are overcrowded. To make matters worse, rock-bottom interest rates have encouraged people to buy, rather than rent, their homes, thus reducing the supply of rented accommodation, which particularly hurts Latinos.

Many Latinos still operate in the cash economy, which means that even the successful ones rarely pass the usual tests for mortgage risk. Unlike, say, Chinese and Korean banks, Mexican banks have been slow to set up in California to help them (though this is now starting).

Why haven't more houses been built— especially given the high prices? Part of the answer is that there are natural barriers to growth. In southern California, houses are going up 50 miles from where your job is, so that you have to commute four or five hours a day. The 100-mile city can go no further. This is “sprawl to the wall”.

But, as Joel Kotkin and Thomas Tseng argue in a study on Latinos and the housing market, the constraint on supply also has a political dimension. Back in 1978 Californians passed Proposition 13, which halved property taxes and constrained their growth. Regardless of its fiscal merits, this has had perverse effects on land use. Local authorities now have a much bigger incentive to give permits to new shopping malls (from which they derive a share of sales tax) than new houses (where property taxes are constrained).

Worse was to follow. The wealth generated in California's late-1990s boom produced an outbreak of

NIMBYism (not in my back yard), which also found expression in California's initiative process. Between 1986 and 2000, 671 local initiatives concerning growth were put to the vote. Around 60% produced victories for the slow-growth lobby.

Environmental pressures also resulted in high fees for developers, an approval process for new construction that is among the most complicated in the country (developers complain it adds about $70,000 to the cost of a single-family home), and an epidemic of lawsuits over construction defects that have made some housing uninsurable. A particular target has been condominiums—jointly owned apartment blocks that are a useful way of putting more people in a limited space. In the mid-1990s, condos accounted for 30% of new houses. By 2000, legal disputes had reduced that to 2%.

Susanne Trimbath of the Milken Institute says that supply has also been cut by a change in the housing business. Rather than just building houses and then trying to find people to buy them, developers increasingly find people to buy houses in advance, getting the householders to pay for construction. This has smoothed out the boom-bust cycle—but it also means that there is not the excess housing on the market you would expect in a recession.

Politically, neither left nor right seems willing to stand against the tide. On the left, Democrats are influenced by the environmental lobby—so, though Latinos tend to vote Democratic, their housing interests are overlooked. On the right, Republicans tend to be “leave me alone” types who want immigrants and their houses located as far away from nice suburbs as possible.

For the moment, the benefits to existing NIMBY householders of not building enough new homes outweigh the economic cost to new migrants. Yet the future of California depends on those migrants, who will increase the state's population to almost 50m in 2025 from 33m now.

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Dealing with al-Qaeda suspects

A necessary evil?

Jul 10th 2003
From The Economist print edition

The Pentagon claims a new form of terrorism needs a new form of justice

Get article background

WHEN the Pentagon announced on July 3rd that George Bush had identified six “enemy combatants” in American custody as eligible for trial before specially convened “military commissions”, it revived a confusing debate which has been running since Mr Bush authorised the creation of such commissions two months after the September 11th terrorist attacks. At times, the Pentagon and its critics seem to be talking about two entirely different things. Pentagon officials insist that any trials held by the new military commissions—now expected to start in the next few months—will be “full and fair”. Lawyers' groups and human-rights campaigners say they will be a travesty.

Defendants, say Pentagon officials, will be presumed innocent until proven guilty. They will be given a lawyer at no expense and will have the right to remain silent. Their lawyer will be able to cross-examine witnesses and present a defence. Their trials will be as open as possible and any convictions will be automatically reviewed by a separate appeals panel.

The Pentagon also insists that the military commissions are better than either American civilian courts—which have already held successful terrorist trials—or America's long-established military courts. The commissions, say officials, will have greater “flexibility” in balancing the demands of a fair trial with the need to pursue America's war on terrorism.

But this “flexibility” is what worries civil-rights lawyers the most. As the detailed regulations issued by the Pentagon earlier this year make clear, nearly all the procedural rights of the accused, which play such a central role in any normal criminal trial, military or civilian, are to be hedged about with caveats. They can be overridden or suspended by the panel of military officers sitting as judges if they agree with the government—ie, their fellow military officers—that this is necessary in the interests of national security.

To dispel any doubt about this, the regulations state categorically that they do not “create any right, benefit, or privilege, substantive or procedural.” The defence secretary can change any of the trial rules at any time. And the Pentagon will also control information during the trial itself. The trial may be open to the press and public, but it can also be closed at any time by the presiding officer or Pentagon officials.

Defendants cannot represent themselves. They must accept a military lawyer assigned to them. They can also have a civilian lawyer, at their own expense, but this lawyer must be an American citizen and must be cleared by the Pentagon for access to classified information.

Even with these qualifications, the civilian lawyer, along with the defendant and public, can be excluded from a trial session if “protected” information—a vaguely defined category much broader than “classified”—is presented by the prosecution. The military lawyer assigned by the defendant has a right to see such evidence, but he cannot communicate it to the civilian lawyer or the defendant without the permission of the presiding officer, who will also be one of the judges deciding guilt or innocence in the case.

Perry Mason, this ain't

Prisoners' rights

Rights to:	US criminal court	Terrorism trials in N Ireland	South African apartheid	US court martial	Military commission
Civil judge	yes	yes	yes	no	**no**
Choose own lawyer	yes	yes	yes	yes	**no**
Remain silent	yes	yes	no	yes	**yes**
Open trial	yes	yes	yes	no	**no**
Jury trial	yes	no	no	no	**no**
Lawyer-client confidentiality	yes	yes	yes	yes	**no**
Know all evidence against you	yes	yes	yes	yes	**no**
Appeal to independent judge	yes	yes	yes	yes	**no**

Sources: US Dept. of Defence; Diplock Commission Report; Cape Town Legal Resources Centre; Human Rights Watch; Amnesty International

There is no guarantee of lawyer-client confidentiality. Communications between defendants and lawyers, state the regulations, can be monitored at any time, apparently without any notification.

Critics argue that, even if defendants learn all the evidence against them, the trials are unlikely to be fair. After months of imprisonment, how many defendants will really trust an American military lawyer? And how far will a serving military officer go in defending an alleged terrorist against charges authorised by his commander-in-chief? Civilian defence lawyers cannot talk about the case, or the trial process, to reporters. Pentagon officials not directly connected to the trial can say what they like.

If a defendant is acquitted, the Pentagon has made clear, there is no guarantee that he will be released. He could continue to be held indefinitely as an "enemy combatant" posing a threat to America. That is a separate "determination", say officials.

The biggest worry for civil-rights people is the notion that defendants have no right of appeal to genuinely independent judges outside the military chain of command. Trial panels will consist of between three and seven military officers, with at least one being a qualified military lawyer. Three-quarters of the panel must vote guilty to convict, and death sentences can only be imposed by the unanimous vote of a seven-member panel. Convictions and sentences will be reviewed by another panel of military officers. The final appeal can be made only to the secretary of defence or the president. By contrast, ordinary American military courts permit appeals to a civilian federal appeals court, independent of the executive branch. The Pentagon's commission regulations explicitly exclude any such judicial review.

On most measures of a defendant's guaranteed rights, the military commissions are far more draconian than other terrorism courts—such as Britain's Diplock courts in Northern Ireland (see table). The Bush administration retorts that the commissions—which are only for non-Americans—are needed to protect information that could be of use to al-Qaeda; and also that the commissions will prove themselves fair in practice.

Regardless of protests so far, Mr Bush seems determined to push ahead with a system of Pentagon-run courts which can be convened anywhere in the world at any time—and which might become permanent. "It's very easy to criticise something if you haven't seen it in action yet," says Major John Smith, a Pentagon spokesman. "Military commissions may come to be seen as a very legitimate and proper way of dealing with international terrorism."

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The reaction from abroad

Just don't kill them

Jul 10th 2003 | LONDON AND SYDNEY
From The Economist print edition

American military justice, seen from overseas

Get article background

"JUSTICE must be seen to be done," said Tony Blair facing uneasy questions in the House of Commons on July 9th about the threatened trials of two Britons held at Guantanamo Bay. His government had earlier asked its closest ally to send any British captives for trial in Britain—and been told no. It is now urging that the military tribunals follow procedures the world can see as fair. Meanwhile, 163 members of parliament have already signed a petition calling for the two Britons to be repatriated.

Both men are Muslims. Moazzam Begg, aged 36, had no known record of religious extremism, let alone terrorism, before he went to Afghanistan with his wife in 2001 and set up a school there; he was arrested in Pakistan. In contrast, Feroz Abbasi, 23, before he left for Afghanistan in the winter of 2000-01 was a fervent attender of a London mosque then run by an extremist cleric.

It is hard to see how the tribunals will help Mr Blair (who already faces taunts of being George Bush's lackey). A report in the *Financial Times* that the prime minister may give his consent "because he fears it would be almost impossible to mount a successful prosecution in Britain" is likely only to infuriate civil libertarians further. An extradition to Britain could pose problems. Any trial would have to follow standard criminal-court procedures. Even charges, let alone evidence and "guilty" verdicts, might be hard to come by; as trials of alleged IRA men have shown, the opportunities for propaganda might be large—and acquittals could annoy Mr Bush.

The Australian government of John Howard has been less troubled by news that a young Australian, David Hicks, 27, of Adelaide, is to be tried. Mr Howard said he had faith in the American justice system—even this version of it, presumably—and that Mr Hicks had confessed to being an al-Qaeda fighter, suggesting there was little more to be said.

However, Mr Hicks's father denies the al-Qaeda admission. Mr Hicks senior recently locked himself into a cage in protest, and has since gone to Pakistan and Afghanistan, to retrace his son's steps for a documentary film. And many other Australians feel their government has failed in its responsibility to a citizen by refusing to have Mr Hicks extradited earlier this year, when the Americans seemed ready to hand him over. Australia's opposition Labor Party has flatly denounced its government's line.

And suppose any of the three men were condemned to death? This would be a nightmare for Mr Blair. Both Britain and Australia long ago abolished this penalty, and both would protest vigorously that it should not be carried out. Though no promises have been made, they could expect to win their point.

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Lexington

Get me to the church on time

Jul 10th 2003
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The Bush administration's marriage-guidance counsellor and the charms of neo-paternalism

HERE we go again. In the wake of the Supreme Court's ruling on *Texas v Lawrence*—better known as the sodomy decision—America's culture warriors are busy recycling their talking points about gay marriage. Liberals think that the ruling proves that gays should be given the same rights as everybody else, including marriage. Aghast, conservatives retort that gay marriage will undermine the foundations of society.

And George Bush? The “compassionate conservative” president, terrified of offending both conservatives and compassionate sorts, has said as little as possible. But on the subject of heterosexual marriage the Bush administration has a lot to say—and a radical agenda. Wedlock, it firmly believes, can promote both social stability and economic well-being. So firmly that it is using welfare policy to encourage the poor to get married.

For many American conservatives there is no more odious word in the lexicon than “paternalism”. Forget Disraeli's one nation, or any other wet British ideas. Members of America's “leave us alone” regiment regard government as the source of all evil: a ravening monster that wants to steal their money, confiscate their firearms and otherwise mess with their lives. For them the purpose of conservatism is to starve the beast to death.

But under Mr Bush the leave-us-alone bunch has been losing ground to what might be called the “neo-paternalists”—a group that includes Christian fundamentalists, Straussian intellectuals and old-fashioned preppies. Mr Bush is not only presiding over a huge increase in the size of government. He is also encouraging the beast to poke its nose into the nooks and crannies of people's private lives. For him politics is not just about shrinking government (a good job, too, given his performance). It is about prodding behaviour in a conservative direction.

The public face of Mr Bush's marriage policy is Wade Horn, the man responsible for families and children at the Department of Health and Human Services. Charming and donnish, Mr Horn could hardly be more different from the blustering self-promoters who have dominated the virtue business for far too long—“Lucky” Bill Bennett and the rest of them. In a previous life Mr Horn was a child psychologist and he has been making the case for marriage for years. When he worked in Washington's Children's Hospital, he encountered large numbers of inner-city children who were clearly psychologically damaged by the absence of a father. He created the National Fatherhood Initiative in order to encourage fathers to

become more involved with their children. Now he is at the heart of the welfare machine.

That machine is whirring more than usual at the moment. Congress is preparing to reauthorise the 1996 Welfare Reform Act, and the White House is trying to add a new ingredient to the pot: $300m a year for programmes to strengthen marriage. These programmes include teaching “relationship skills” to unmarried couples who are expecting a baby, and providing “marriage-skills training” to married people who want to get on better.

Mr Horn's case for promoting marriage rests on an undeniable fact: the erosion of marriage is creating social problems. When Daniel Patrick Moynihan gave warning, back in 1965, that the breakdown of the black family was a social catastrophe in the making, only a third of black children lived in one-parent families; today a third of all children live in one-parent families, and two-thirds of all black children. These children are more likely to live in poverty, depend on welfare, take drugs or end up in jail than children from two-parent families.

An ongoing study of “fragile families”, conducted jointly by Princeton and Columbia Universities, shows that around three-quarters of non-married mothers are involved in a reasonably stable relationship with their partners when their child is born. Most of the fathers are good marriage prospects, with a median income of $17,500 a year and no serious problems with drink or drugs. Robert Rector, a welfare guru at the conservative Heritage Foundation, calculates that, if the mothers tie the knot, only 17% of them remain poor; if they remain single, 55% of them will.

Do you need marriage-skills training?

All the same, isn't there something a little Orwellian about a bureaucrat offering “marriage-skills training”? The neo-pats retort that America already has a huge welfare state currently weakening marriage. Three-quarters of the $200 billion a year the state gives to poor families with children goes to single-parent families. Indeed, the system discriminates against marriage by penalising poor mothers who marry men with jobs. “This is not about expanding government,” says Mr Horn. “It is about doing it better.” Moreover, he is hardly advocating shotgun weddings. Most poor mothers are romantically involved with their child's father when the child is born. Most hope to get married some time in the future. This is merely helping to translate a vague intention into a firm commitment.

In fact, Mr Horn's real problem may not be Big Brother but Little Money. How on earth can a $300m programme make a difference to a policy that is pumping $150 billion in the opposite direction? The 1996 Welfare Reform Act was supposed to encourage both work and marriage, but many states continue to make it much harder for two-parent families to get public assistance than single-parent ones.

So Mr Horn clearly has his work cut out. But his quiet toiling away is a sign that Mr Bush would still like to rescue his reputation as a compassionate conservative. What could be more compassionate than helping the poor off welfare? And what could be more conservative than trying to encourage marriage? The only trouble is putting this into practice. Conservatives have long criticised liberal paternalists for overestimating the power and precision of social engineering. The same criticism could also be levelled against the neo-pats.

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Mexico's congressional election

Putting the brakes on change

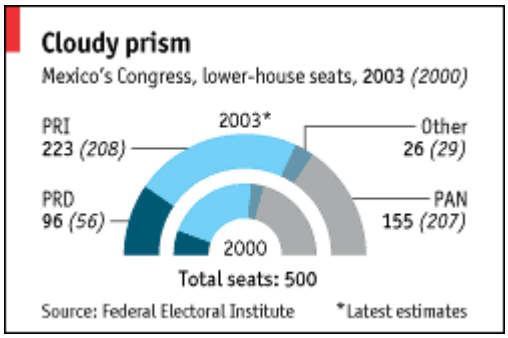
Jul 10th 2003 | MEXICO CITY
From The Economist print edition

If democracy is to work, the opposition has as much to prove as President Fox

Get article background

THERE were two main losers in last Sunday's mid-term elections in Mexico. The first was President Vicente Fox's conservative National Action Party (PAN). The second was democracy itself: only 41% of voters bothered to turn out to choose the lower house of Congress, a disappointing figure for a country that has staked so much hope on its transition to a pluralist democracy. But if it was a bad—and perhaps fatal—result for Mr Fox's government and its stalled agenda of reforms, neither was it an especially good one for any of the opposition parties.

The PAN's campaign slogan was “Take the brakes off change”. But the voters have ended up pressing the brake pedal right to the floor. Many of those who voted for the radical changes that Mr Fox promised in 2000 tell pollsters they are disappointed. This time, they stayed at home. The PAN's share of the national vote was only 30.5%, down from 40% in 2000 when it was buoyed up by Mr Fox's presidential victory. Until only a few months ago the PAN had been confident of winning the congressional majority which had eluded it in 2000. Instead, it lost about a quarter of its seats in the lower house (see chart). It also lost the governor's race in the state of Nuevo Léon, previously a stronghold.



The election's self-proclaimed victor was the formerly ruling Institutional Revolutionary Party (PRI). It strengthened its position as the largest party in Congress. But at 35%, its share of the national vote was down slightly from 2000. It won Nuevo Léon, but lost the state governorship in San Luis Potosí to the PAN. But the election did show that the PRI is still the only truly national party. Because its vote is distributed evenly throughout the country, its comparatively modest overall share stacks up into a disproportionate number of congressional seats.

Not so for Mexico's third party, the left-wing Party of the Democratic Revolution (PRD). It scored an overwhelming triumph in local elections in Mexico City. Thanks to the popularity of Andrés Manuel López

Obrador, the capital's PRD mayor, the party swept 13 of the 16 district councils in the city. That will provide Mr López Obrador with a solid platform for a presidential bid in 2006. The PRD almost doubled its seats in the federal congress, too. But that was mainly because ill-judged alliances had robbed it of seats in 2000. Its share of the vote fell slightly this year.

The election betrayed just how concentrated the PRD's support is, in ten states (most in the centre and south). In the other 21, it won less than 10% of the vote. Party officials admit that if Mr López Obrador is to become president, the PRD will have to work far harder to broaden its support. For all the parties, the main task is to win the confidence of the six voters in ten who didn't bother to turn out. But the prospects of doing so are not good. The election produced the third consecutive Congress in which no party has an overall majority. Since 2000, Mr Fox has constantly wrangled with a legislature dominated by the PRI and PRD. As a result, his government has achieved little.

All politicians are aware that this sterile deadlock is what partly explains the voters' disillusion. Many have tried to sound constructive this week, talking of reaching cross-party agreements to get some urgently needed reforms through. But will this new resolution last beyond the end of next week? Some analysts think not, and are already writing Mr Fox off as a dead—rather than merely lame—duck. After all, by blocking just about everything Mr Fox has attempted, the PRI has scored a tactical success, damaging the PAN electorally.

But others argue that to boost its national appeal, the PRI must show that it can do more than just sabotage Mr Fox. Both stances have defenders within the PRI itself. Because the party's strategy has always been to embrace such a broad centre ground, it is inevitably split on most policy issues. That is why it avoided any semblance of national policy commitments during the campaign.

In its first response to defeat, the government seemed suitably humble. Santiago Creel, the interior minister, sketched out an agenda that he thought might find cross-party support. He mentioned a bill to allow Mexicans living abroad to vote and another to end the ban on re-election of congressmen, which most politicians now think outdated. The government also wants to reform the criminal justice system. These proposals could find support from both the PRI and the PRD.

But economic reform is far trickier. Mr Fox wants to liberalise Mexico's economy, the PRD favours economic nationalism, and the PRI does the splits between the two. Mr Creel talks of another effort to reform the tax system, and of opening up telecoms to more competition. The most urgent, but most opposed, measure is to allow private investment in energy.

Mr Creel also hinted at cabinet changes. Stitching together coalitions for each piece of legislation is a job for gritty party managers, rather than the more aloof President Fox. That might make him less relevant over the next three years. But if the parties start to address Mexico's problems, the electorate will not care too much about that. More of them might actually turn out to vote next time.

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Argentina's armed forces

Past crimes

Jul 10th 2003 | BUENOS AIRES
From The Economist print edition

Re-opening the “dirty war”

Get article background

EPA

The nightmare that won't go away

EVER since democracy returned in 1983, Argentina's governments have struggled to heal the wounds left by the country's “dirty war” involving the security forces and leftist guerrillas in which up to 30,000 died, most of them civilians murdered by the armed forces. Alone among the South American dictatorships of the 1970s, Argentina's faced some retribution. After trials in 1985-86, nine generals and admirals (as well as some guerrilla leaders) were imprisoned. But in the face of military unrest, governments then backtracked—until now.

The new president, Néstor Kirchner, promises to reform his country's discredited institutions. The army is high on his list. On taking office in May, he purged dozens of senior officers, many of whom served the dictatorship. Now, Mr Kirchner is set to repeal a decree blocking the extradition of Argentines to face human-rights trials abroad. Instead, he wants the courts to decide each case. The issue is a live one: last month, Ricardo Cavallo, a former Argentine naval officer, was extradited from Mexico to face trial in front of Baltasar Garzón, a crusading Spanish judge.

Mr Kirchner is also wielding his broom against the Supreme Court. He has secured the resignation of one judge, and wants others to go. The court is due to rule on two 1989 laws which put a stop to the trials of military officers. The old court was likely to uphold them. Mr Kirchner's candidate for the vacant spot on the court is on record as saying that the laws are unconstitutional. Later this year, they may be struck down.

All this has gone down badly in the barracks. On July 7th, officers received the president in stony silence at a “camaraderie” dinner. Mr Kirchner told his audience that “everyone has to accept responsibility for what he did.” He clearly reckons he can afford to play tough. The armed forces are a tiger with few teeth: they have been starved of funds for two decades, and are still unpopular. Polls suggest that two out of three Argentines favour scrapping the laws halting further trials, as well as the ban on extraditions.

But even if that happens, it is unlikely to result in a procession of officers through the courts, according to Víctor Abramovich of the Centre for Legal and Social Studies, a human-rights group. Over 90% of the army enlisted after the end of the dictatorship. Many of the accused officers have died of old age, as have many witnesses. Rather, the repeal of the laws would be a symbolic break with the past, he argues.

Others disagree. This week, Antonio Bussi, a retired general whom Mr Garzón would also like to try in Spain, was narrowly elected as mayor of Tucumán, a provincial capital. His chief opponent is the son of a senator who “disappeared” in 1976. The “dirty war” will continue to cast a shadow in Argentina for a while yet.

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Venezuela

Another Cuba?

Jul 10th 2003 | CARACAS
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An army of foreign volunteers has the opposition worried

Get article background

HUGO CHÁVEZ, Venezuela's president, once remarked that his country is steering towards “the same sea of happiness” as Cuba. However hard Mr Chávez also insists that his “revolution” is inspired by an independence hero, Simón Bolívar, rather than by Karl Marx or Fidel Castro, some of his opponents are not convinced. The alleged “Cubanisation” of Venezuela is an issue that will not go away.

There is no dispute that Mr Chávez has a close personal relationship with the Cuban leader. Mr Castro has visited Venezuela three times since Mr Chávez took office in 1999. He has addressed the National Assembly, celebrated his birthday near the fabled Angel Falls, and sung a duet with his Venezuelan counterpart on the latter's weekly television and radio show. Mr Chávez makes frequent unscheduled stopovers in Havana, most recently after a visit to Colombia at the end of June. But does all this presage, as the opposition argues, an attempt to create a “second Cuba” on the mainland of South America?

Although he is a former army officer who tried to seize power in a failed coup in 1992, Mr Chávez, unlike Mr Castro, is democratically elected. He has concentrated power in his own hands. But in practice, he has not restricted basic freedoms (though several bills before the assembly might do so). Broadly speaking, he has remained within the confines of a mixed economy. Even so, the opposition's fears may not all be anti-communist hot air.

Under an agreement signed in 2000, Venezuela sends energy-short Cuba 53,000 barrels a day of oil on exceptionally favourable terms. In turn, Havana has sent—altruistically, it claims—hundreds of teachers, doctors and sports instructors to Venezuela. They have designed a literacy programme and are staffing a health scheme, both in poor neighbourhoods.

Venezuela's teachers' and doctors' associations cast doubt on the qualifications of the Cubans. They wonder aloud why Venezuela, with thousands of unemployed professionals, needs to import foreigners. Officials counter that Venezuelan doctors and teachers lack the community spirit needed to work among the poor. They say the growing anti-Cuban campaign is politically inspired; they reject the claim that “volunteers” sent by Havana are spies, or communist indoctrinators.

The opposition's fears are heightened because much of the private sector faces extinction. In the aftermath of an abortive opposition attempt to strangle the government with a two-month strike in December and January, Mr Chávez decreed price and exchange controls. Starved of dollars, and obliged in some cases to sell at less than cost, producers and importers are outraged that the government is using its burgeoning foreign reserves (now at $18 billion) to import and distribute itself basic goods such as beef, chicken and flour.

Projected into the not-too-distant future, these trends would leave Venezuela with a shrunken private sector, mainly of small and micro-enterprises dependent on government handouts. Multinationals would run a few key businesses (such as parts of the oil industry) in association with a powerful government. Not Cuba, perhaps—but not far off either.

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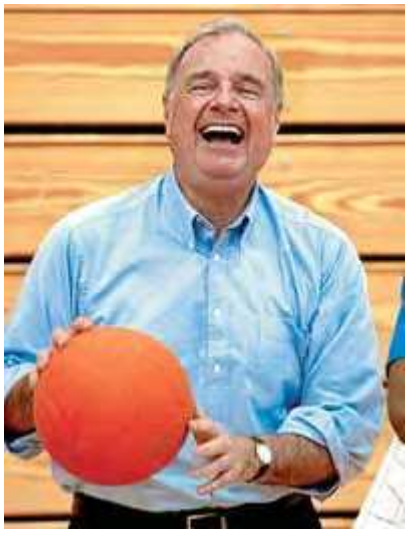
Campaign finance in Canada

Closing the private purse

Jul 10th 2003 | OTTAWA
From The Economist print edition

A clean-up with mixed motives

Reuters



Martin will be reduced to sponsored hoops

IN SOME ways Jean Chrétien's last summer as Canada's prime minister is proving less serene than he might have hoped. Most of his Liberal Party's caucus of MPs, and many of his ministers, have now switched their loyalties to his likely successor, and bitter rival, Paul Martin. When they return to Ottawa in the autumn, the caucus may prove obstreperous, perhaps blocking social measures, such as an overhaul of the Indian Act. Mr Chrétien intends these to be part of his legacy (he plans to step down next February). Instead, his last year may be remembered for another radical measure—one that has caused some of the Liberal discontent.

Late last month, Mr Chrétien secured approval of a law that imposes a sweeping ban on all but the smallest political donations by businesses or trade unions. Instead, private individuals will be encouraged to contribute more to politics through bigger tax breaks. But most of the shortfall will be picked up by taxpayers through an elaborate system of public finance, based on votes at previous elections. A one-off federal payment to the parties of C$20m ($14.8m) will cover the transition costs of switching to the new system next year.

Mr Chrétien's government has been tainted by scandals in which big Liberal donors have received favours, including juicy contracts which were not put out to tender. One of the more nagging cases implicated the prime minister himself; another is the subject of police investigations which could embarrass Mr Chrétien even in retirement. The prime minister denies that those controversies inspired the law. The problem, he says, is a public perception that influence is for sale, which breeds cynicism and mistrust of politicians.

The law applies to political parties, their leadership contenders and their election candidates. Its main beneficiaries are likely to be opposition parties such as the right-wing Canadian Alliance and the separatist Bloc Québécois. Neither raises a fraction as much corporate cash as the Liberals. Each will now receive millions of dollars of public money. And the left-wing New Democrats will no longer have to depend on labour unions for cash.

The Alliance still voted against the law. But the sharpest opposition came from Mr Chrétien's own ranks. The Liberals have become the party of corporate Canada, and have most to lose financially from the new rules. “Dumb as a bag of hammers,” was the verdict of Stephen LeDrew, the Liberal Party president, a supporter of Mr Martin. (Mr Chrétien's right-hand man returned the compliment by sending Mr LeDrew a bag of hammers, with a note encouraging him to use them to “knock some sense into your head”.)

To his critics, the law looks plain hypocritical. In a decade as prime minister, Mr Chrétien has made a regular ritual of big-donor dinners, bringing in as much as C$1m a night. Now, his successors will be denied this source of wealth. Mr Martin is even closer to Canadian business than Mr Chrétien. Whether or not it succeeds in cleaning up the image of Canadian politics, the new law is likely to make life difficult for Mr Martin. That just might have been the intention.

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Bolivia

Fire in the Andes

Jul 10th 2003 | LA PAZ
From The Economist print edition

A fight over land reform is hotting up

IN LARGE and sparsely populated Bolivia, it might be thought that land should not be a problem. But it is. Only 6.5% of the country is suitable for farming, and the best of this land has long since been taken. Half a century ago, a land reform shared out much of the highland plateau known as the Altiplano among peasant farmers, slowing the rush to the cities. But now land hunger is again causing unrest.

This month, protesters set fire to pasture on the Altiplano near La Paz, the capital. They occupied a large dairy farm which once belonged to the president's brother-in-law. These actions were staged by the Movimiento Sin Tierra (MST), a newish group inspired by Brazil's militant (and successful) landless movement. As in Brazil, its ranks have been swollen by the urban unemployed.

The government of President Gonzalo Sánchez de Lozada has promised to hand out public land, but has been slow to do so. But land alone is not much help without investment in schools, health posts, water supplies and roads. “People can't be parachuted into isolated areas with just a pickaxe”, points out Miguel Urioste of Fundación Tierra, a research institute.

While much of the Altiplano is devoted to subsistence farming, commercial farming, of soya and cotton, is booming in Bolivia's eastern lowlands. The MST's protest squats had hitherto been confined to this area, on farms it claims are lying idle. Under past dictatorships, huge tracts of land were handed out to army officers and their political cronies. In theory, the government is committed to recovering this land. But it is dragging its feet—so as not to harm its landowning friends, claims the MST.

In his first presidency, from 1993-7, Mr Sánchez passed a law to modernise land registries and regularise chaotic and missing legal titles. That should have speeded up land reform. But the government agrarian-reform agency is notoriously highhanded and inefficient. Ironically, Moira Paz, the minister now charged with sorting out this mess, is the daughter of the president who carried out the 1950s land reform. Perhaps she should finish the job her father began.

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Award

Jul 10th 2003
From The Economist print edition

Michael Reid, our Americas editor, has been awarded a Maria Moors Cabot Prize for outstanding reporting on Latin America by Columbia University's Graduate School of Journalism.

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Hong Kong and China

In the dock

Jul 10th 2003 | BEIJING
From The Economist print edition

Reuters

China's man in Hong Kong has been humiliated by popular protest

Get article background

FOLLOWING a huge public display of displeasure with his leadership, Hong Kong's chief executive, Tung Chee-hwa, has been forced to make big concessions to his pro-democracy critics. By watering down a controversial internal-security bill and then delaying plans to present it to the legislature, Mr Tung has sought to defuse a mounting political crisis. But by doing so he has badly dented his authority, and shaken China's confidence in its ability to control the territory. The crisis shows no sign of abating.

China, which appointed Mr Tung as Hong Kong's first post-colonial leader six years ago and gave him a second term last year, is watching anxiously. Only a couple of days before Mr Tung's aides revealed, in the early hours of July 7th, that the legislation would be postponed, a senior Chinese lawmaker had said the bill should be submitted for final debate by the Hong Kong legislature on July 9th as originally planned. By changing his mind, Mr Tung demonstrated that, despite its authoritarian political system, Hong Kong can be swayed by people power. This is not a trend China wishes to encourage. Hence, officials in Beijing have ordered the mainland media to say nothing about the protest by half a million Hong Kong citizens on July 1st that led to Mr Tung's predicament.

Especially worrying for China is the break-up of the once tight-knit group of pro-China politicians in Hong Kong upon whom the stability of Mr Tung's rule has depended. It was the late-night resignation from Mr Tung's cabinet on July 6th by James Tien, the head of the Liberal Party—largely made up of business people, many of whom have close links to China—that pushed the chief executive to make his dramatic climbdown in the small hours, after an emergency meeting of his cabinet. While preparing to take over Hong Kong from the British, China was careful to make political arrangements that would ensure that Beijing loyalists would prevail over those demanding full democracy. Now those arrangements are unravelling.

Mr Tien, who is also a legislator and an adviser to China's parliament, said more time was needed for discussion of the bill, despite Mr Tung's decision last Saturday to make substantial revisions. These included dropping provisions that would have allowed the banning of groups that are proscribed on the mainland and would have given the police sweeping powers of search. Mr Tung also conceded that journalists could publish Chinese state secrets if it was in the public interest. Without the Liberal Party's

support in the Legislative Council, Mr Tung could no longer be sure of winning. His problems may be further compounded if the other legislator in his cabinet, Tsang Yok-sing, also quits. Mr Tsang, who heads the pro-China Democratic Alliance for the Betterment of Hong Kong, has not ruled that out.

China once regarded Hong Kong's middle-class professionals as natural allies, believing that they ultimately cared more about preserving stability and making money than about democracy. But the July 1st protest profoundly changed that assumption. Many of the participants were traditional supporters of the Liberal Party. Mr Tien's decision was probably made with an eye to his political future. Similarly, Mr Tsang must now be worried. His party has strongly supported the bill. If it continues to do so, it risks losing the considerable gains it made in the 2000 polls, when it captured nearly 30% of the vote, compared with about 35% for the Democratic Party, a strong critic of China.

Mr Tung's proposed changes to the bill addressed key concerns raised by the legislation's opponents. But the demonstration was directed as much against Mr Tung himself as against the bill. Even a few pro-China politicians are now suggesting it might be time for Mr Tung to step down. The chief executive has made it clear he has no such plans. “The administration is facing some huge challenges,” he conceded on July 9th, shortly before tens of thousands joined a candle-lit vigil outside the legislature to protest against the security bill. But Mr Tung said his administration was united and he was confident it could “ride out these challenges”.

Many observers expect Mr Tung to try to win public support by shuffling his cabinet. But pro-democracy politicians would still keep up the pressure. Scrapping the bill and getting rid of Mr Tung are only short-term goals. The real aim is to persuade the government to allow the chief executive and the legislature to be elected by universal suffrage after 2007. Although Hong Kong's constitution allows this, Mr Tung has resisted debate on the subject.

The dilemma for China is that if it asks Mr Tung to step down (in a behind-the-scenes, face-saving way, of course), it would have to appoint either a tougher figure who might inflame public sentiment by ignoring demands for political change, or a more conciliatory one who might allow Hong Kong to break free from its moorings to the mainland Communist Party. Officials in Beijing are clearly at a loss—unwilling either to give clear endorsement of Mr Tung and his policies or to suggest it might be time for him to move on. China would prefer to keep Mr Tung in place, weakened though he is, rather than concede that its choice was wrong. While Beijing officials fret and dither, Hong Kong finds itself in uncharted waters.

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China

Boom town blues

Jul 10th 2003 | YULIN, SHAANXI PROVINCE
From The Economist print edition

Officials seize private oil wells

Get article background

AN OIL rush that has brought unprecedented wealth to Shaanxi Province, a remote and backward area of China, has come to a sudden and traumatic end. The local government's seizure in recent weeks of hundreds of privately controlled oil wells into which hundreds of millions of dollars have been sunk has triggered protests by thousands of investors and clashes with the police.

Several prominent liberal scholars and former officials in Beijing have taken up the investors' grievances, arguing at a recent symposium and in petitions that the events in Shaanxi have undermined the Communist Party's efforts—the so-called “Go West” policy—to nurture the private sector and encourage investment in the entire impoverished region. The central government has made no public comment. It has encouraged efforts to bring order to Shaanxi's chaotic and fragmented oil business, which suffers from widespread corruption and pollution as well as considerable waste. However, it is thought that the leadership considers that Shaanxi officials have gone too far and wants them to reach a compromise with the region's more than 1,000 oil-extraction companies.

The consequences of letting the problem fester could be considerable. The oil wells are spread across 15 counties in two prefectures of northern Shaanxi: Yanan, where Mao Zedong established his headquarters in the 1930s, and neighbouring Yulin. Many of the investors are locals who have mortgaged their homes and borrowed at usurious rates to buy shares.

On May 12th in Ansai, in Yanan prefecture, police clashed with about 400 investors whose wells had been seized without compensation in March. Dozens were injured. On June 16th in Jingbian county, in Yulin prefecture, scuffles broke out between police and investors who had reclaimed their oil wells. Later, some 4,000 investors from Yulin converged on the provincial capital, Xian, to petition the leadership, but without success. Since early this month, shareholders have staged daily sit-ins outside the Jingbian county government headquarters. Others in neighbouring Dingbian county have been playing cat and mouse with officials trying to guard the wells, regaining some while being forced from others.

Local officials have justified their decision partly on the basis of a directive from Beijing in 1999, ordering a halt to private involvement in oil extraction. Investors point out that the document was secret and that many of them signed their drilling-rights contracts with local governments after it was issued. In any case, they say, foreign private companies can do such business in China, so why not Chinese? The contracts, they argue, should have more legal weight than a confidential document. But local officials have ordered courts not to accept any cases relating to violation of oil contracts. The Shaanxi government may also have been afraid that, if it failed to act, the central government might pass the rights to exploit the oil fields to a state oil company. Before 1994, northern Shaanxi's oil had been partly under the control of the China National Petroleum Corporation.

Many investors have been offered compensation that would amount to at most 20% of what they put in. This would leave many thousands bankrupt. One investor recalls the famous long march of 1934-35 that brought Mao to the area. “When our Red Army soldiers ate ordinary people's rice,” he says, “even if there was no one there to receive it, they would leave a little silver as payment. Now we have invested this

huge amount of money and they just take it away at a whim.”

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Japan's economy

A bit of bounce

Jul 10th 2003 | TOKYO
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But not yet a real recovery

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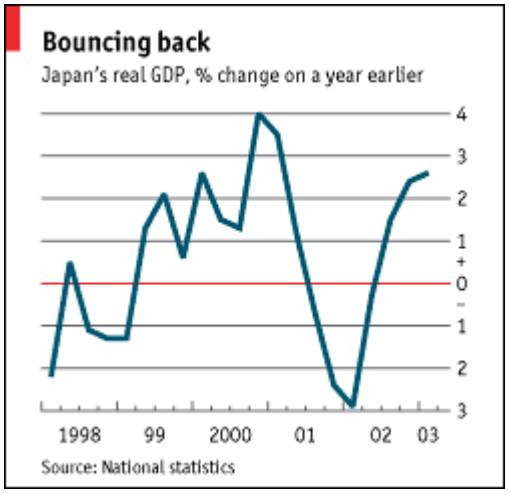

AFTER more than a decade of stagnation, a little good news goes a long way in Japan. Some encouraging economic signs over the past few weeks, therefore, have made many people in Tokyo giddy with optimism. The stockmarket has been rallying, companies' profits are up, wage income is increasing, and business investment looks set to enjoy a healthy rise. This does not add up to a solution for Japan's structural problems; as the past has shown, a small cyclical rebound is not enough to pull the economy out of its rut. Yet it does seem that this year is shaping up to be less gloomy than the previous two.

Stockmarket investors certainly like what they see. After hitting a 20-year low in late April, the Nikkei 225 index has risen by 30%. On June 8th, it briefly topped the 10,000 mark for the first time since last August. This rally is being driven partly by looser monetary policy in rich economies, which has helped equity markets worldwide. In America, Europe and elsewhere shares have risen sharply since the war in Iraq more-or-less ended. Japan lagged behind, by several weeks. But even struggling along after the rest of the world is a small triumph for Japan these days.

Besides, some happy developments at home have given spirits a lift. For one, the painful but cost-trimming job cuts of the past couple of years seem at last to be producing results. In the fiscal year that ended in March, a collection of 1,600 non-financial companies tracked by the *Nikon Keizai*, a business daily, earned roughly Y5.23 trillion ($44.4 billion) in combined net profit, after losing money the year before.

Although those job cuts were necessary, it is hard to reverse a deflationary spiral just by trimming costs. If most firms are sacking workers, incomes and therefore sales and new investment are all liable to suffer. So it is cheering that in fact domestic demand and incomes seem to be rising as well. Real GDP grew by 2.6% in the first quarter of 2003. A 2.5% monthly rise in industrial output in May suggests the second quarter will also turn in decent growth.

Both employment and wages have risen lately, and large firms are planning to increase summer bonuses by an average of 4.3%. Best of all, they are confident enough to make reasonably optimistic investment plans. The most recent quarterly Tankan survey of business sentiment, taken in June, forecast a 4.9% recovery in large firms' capital expenditures.

All this suggests that, for the time being at least, the pace of deflation may be about to slow a bit. There are signs that prices of durable goods are falling less rapidly, and consumers seem to expect deflationary pressures to ease. That may be one reason why bond prices have fallen sharply lately, though yields remain very low.

It would be nice if Japan's policy-makers could seize this opportunity to make a concerted push for reform and recovery. That would give a small bounce a chance of developing into a long, healthy expansion. But don't count on it. Since Toshihiko Fukui became its governor in March, the Bank of Japan has loosened policy a bit, but not nearly enough. Signs of genuine co-operation between the bank, Junichiro Koizumi's cabinet and the finance ministry remain depressingly rare. So enjoy the good news,

and hope it lasts.

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Television in India

A clearer picture

Jul 10th 2003 | DELHI
From The Economist print edition

And cheaper too, hope Indian viewers

CABLE television has been one of the most unregulated parts of India's economy since it was introduced in the early 1990s; but the government is now tidying things up. The country has more than 30,000 independent cable-TV operators—"cable-wallahs"—who have strung cables along trees and telegraph poles to link their satellite dishes with about half the country's 80m television sets. Charges have been low, ranging from 50 rupees ($1) a month in small towns for about 20 free channels, to 250-400 rupees in large cities for a mixture of 70 or more free and pay channels from satellite broadcasters.

This cheap, if haphazard, system might seem acceptable in India, despite unreliable service and gang warfare both between cable-wallahs and with multi-system operators who franchise the small operators in large cities. In fact, it isn't. Broadcasters say the operators under-report subscriber numbers by as much as 80%, and the government says they declare only a tenth of their income for tax. Broadcasters are accused of over-estimating viewer figures to impress advertisers, and the cable-wallahs blame them for unreasonably raising prices, and blacking out channels when they object. Customers moan that cable-wallahs, with monopolies in many areas, charge too much for blurry pictures.

So six months ago the government announced a "conditional access system" to start on July 14th in India's four biggest cities, led by Delhi and Mumbai, where there are 5m-6m homes with cable television. Access to 30-odd free channels would cost 72 rupees plus tax (say $2 in all) per month. Viewers wanting pay channels would have to buy or hire a set-top box that would record what they bought.

This has upset broadcasters, who will no longer be able to claim high viewer figures for their programmes because the boxes would produce precise numbers. But, pushed by the cable operators and by businessmen who had begun to import the boxes, the government demanded an agreement. Prices have come down steeply in the haggling, and virtually all viewers should pay less than they do now. Alas, it has now been discovered that hardly any set-top boxes are yet available. So the new deal is now due to stagger into operation between September and December.

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Sri Lanka

Rescuing the peace

Jul 10th 2003 | COLOMBO
From The Economist print edition

Fears of a return to war

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ONCE again the Sri Lankan government has turned to Norway to try to rescue its endangered peace deal with the Tamil Tigers. Norway brought the two sides together 18 months ago, getting them to agree to a truce in the civil war in which more than 65,000 people have died in some two decades of fighting. In April the Tigers suspended talks with the government that were designed to lead to a “homeland” for the minority Tamils in the north and east of the island. On July 8th a Norwegian envoy, Jon Westborg, travelled to Kilinochchi, in Tiger-held territory, to ask the Tigers their conditions for re-starting the talks.

Publicly, the Tigers have said that they are waiting for details from the government about how a proposed homeland would be administered. But the real differences between the two sides may be insurmountable. The Tigers want an international ban on their organisation to be lifted. It has been lifted in Sri Lanka, but remains in place in the United States, the European Union and elsewhere. The Tigers' bases in these countries have been shut down and their fund-raising activities made illegal. As a terrorist organisation, its known funds, estimated to be around $4 billion, have been frozen. The Tigers blame the Sri Lankan prime minister, Ranil Wickremesinghe, for the international bans, but he cannot get them lifted. Nor, it seems, can the Norwegians.

The Tigers run a shadow Tamil statelet, which they call an Eelam, in the areas under their control in the north and east. Velupillai Prabhakaran is head of state and commander-in-chief of the armed forces. The statelet has a flag, a national anthem and a police force. It also dispenses summary justice. Taxes are imposed, which the Colombo government calls extortion.

To give this statelet legitimacy in Sri Lanka, the Tigers are keen to have an interim administration in the region. They believe that it will be a stepping stone to a separate state they still consider desirable, despite Mr Prabhakaran's declaration that full independence is no longer the Tigers' aim.

But an interim administration must not dilute the unitary nature of the Sri Lankan constitution. Defence, internal security, foreign affairs, monetary policy and the legal system would continue to remain in the hands of the central government. Mr Wickremesinghe knows that he could not tamper with these elements. However, if the Tigers are unsatisfied with what the government offers, there are fears they will scupper the peace talks and resort to war again. Four previous attempts to end the war have failed. There are reports from their strongholds in Jaffna that the Tigers are preparing for such an eventuality.

If it is any comfort to Mr Wickremesinghe, he has won the support of the international bankers and donors for his efforts to make Sri Lanka an open-market economy. At the next round of peace talks, probably later this month if Mr Westborg's efforts are successful, Mr Wickremesinghe will draw confidence from knowing that at least he is doing something right.

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Australia

Drying out

Jul 10th 2003 | ADELAIDE
From The Economist print edition

The country's main river system is faltering

THE mouth of the Murray, Australia's principal river, has dried up. For only the second time since European settlement 215 years ago, the river system that feeds most of the country has stopped flowing to the sea. The depleted Murray's salt levels are rising, leaving Adelaide, one of Australia's biggest cities, facing a big problem: its water supply will be undrinkable in 20 years unless a way can be found to restore the river to health.

Australians have been reminded of the fragility of life in a dry continent. A drought that that has been ravaging much of eastern Australia for the past 18 months is only part of the problem. A bigger one comes from the relentless demand by farmers for water from the Murray and its main tributary, the Darling River, to irrigate their crops. The Murray-Darling basin, as it is known, covers an area the size of France and Spain, stretching through four states in eastern Australia. It supplies almost three-quarters of Australia's farm irrigation water. And it can no longer cope.

South Australia, where until recently the Murray flowed into the Southern Ocean at Coorong, is the state at the end of the line. With little but desert and dry rivers to its north, Adelaide, the capital, depends entirely on water piped from the Murray more than 100km (60 miles) to the east. People in Coober Pedy, a mining town in the middle of desert, reckon their water, pumped and treated from ancient underground deposits, tastes better than Adelaide's. South Australia's minister for the Murray River, John Hill, says its rate of flow is half that needed to sustain it environmentally. From this month, irrigators in South Australia will have their water allocations cut by one-fifth; in October each state taxpayer will start paying a levy to raise A$20m ($13m) a year. The money will go towards buying extra water from upstream and projects to restore the flow.

Victoria, New South Wales and Queensland, the more populous states that draw on the Murray-Darling system more heavily than South Australia, guard their usage jealously. The Murray-Darling Basin Commission, a regulatory body comprising the state and federal governments, was formed only in 1988, despite stark evidence of land degradation and salination related to over-use of the rivers stretching back decades. Don Blackmore, the commission's chief executive, says it pumps 1,100 tonnes of salt out of the river each day, and is about to spend A$67m to increase that by 700 tonnes a day.

Each state has a separate system for farmers to trade allocated water rights from the rivers with neighbours, but not across state borders. Some reformers argue that nothing short of an amendment to Australia's constitution, giving Canberra total power over the river system, will save it. Meanwhile, dredges are pumping away the sand that has turned the Murray's mouth into a series of brackish ponds. Even with heavy rains upstream it is not expected to open again before September 2004. Unless Australians come up with a tougher regime to manage their precious river, Mr Blackmore expects the mouth to go on closing three years out of 10.

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The travelling toads

Crocs crocked

Jul 10th 2003 | EAST ALLIGATOR RIVER, NORTHERN TERRITORY
From The Economist print edition

Violence in Kakadu

A CROCODILE opens its jaws as a boat full of tourists passes. The croc may be thinking of its lunch; it may be yawning, as the aboriginal boatman suggests. Or it could have just swallowed a cane toad. Crocodiles and other wildlife in the Alligator River system draw thousands of tourists each year to Kakadu National Park, on Australia's northern tip near Darwin. A few tourists who swim in these rivers do not come out alive. But now the people-eating crocodiles are meeting their own unlikely match in the form of Australia's most prolific pest, the cane toad.

The toads were introduced from South America, via Hawaii, in 1935 in a bid to wipe out beetles that were devastating Queensland's sugar cane industry. This attempt at biological eradication failed. The beetles lived high in the cane, and the toads proved not to be climbers. Since then they have done nothing but breed and travel. This year they were seen for the first time in Kakadu. The toads release a lethal toxin from glands on their heads when they are attacked. At least one crocodile in Kakadu and several more in the Katherine River to the south have died after eating the toads.

There is more sympathy for quolls, small spotted marsupials that are dying within seconds of pouncing on the toads. Some 60 quolls have been shipped to islands off the nearby Arnhem Land coast to save them from extinction. The survivors may return if the toads can be eradicated. But after their long march from Queensland they are not going to stop at Kakadu.

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George Bush visits Africa

Making new friends, gingerly

Jul 10th 2003 | PRETORIA
From The Economist print edition

AP

Africa and America get to know one another

GEORGE BUSH enjoyed a whirlwind safari this week. He saw an old slave-trading post in Senegal, toured a game park in Botswana, shook hands with several African presidents and was expected to visit an AIDS project in Uganda. In Senegal, he described slavery as “one of the greatest crimes of history”, which may make him slightly less unpopular among black American voters. But his main concern was with Africa's current problems, rather than its historical ones.

The most pressing of these was the civil war in Liberia, which everyone is asking America to resolve. Mr Bush repeated an earlier demand that Charles Taylor, Liberia's warlord-turned-president, spare his country further bloodshed by taking up Nigeria's offer of comfortable exile. Mr Taylor has agreed to go, but won't say when. He argues, with seeming reason, that it would invite chaos if he were to step down before a peacekeeping force arrives in Liberia. Many Liberians, however, suspect that he has no intention of surrendering power unless forced to.

It is a measure of how loathed Mr Taylor is that the entire African Union, the pan-continental gathering of governments that met this week in Mozambique, wants him to go. This is an organisation that regularly speaks up for Zimbabwe's president, Robert Mugabe, but Mr Taylor's backing of murderous rebels in three neighbouring countries puts him beyond the pale. West African governments say they will send 3,000 peacekeepers to Liberia but hope that America will provide money, logistics and leadership.

Mr Bush is still considering whether to send American troops. On July 7th, a small American military team arrived in Monrovia, the Liberian capital, to assess the situation. At one point, on their way to a refugee camp, they were stopped and forced to turn back by Mr Taylor's soldiers. But mostly, they were met by chants of “No more war” and “We want Bush”.

Regime change seems much less imminent in Zimbabwe. Mr Mugabe gave himself and his ministers pay rises of several hundred per cent this week, which he would doubtless argue is only fair given that inflation is over 300%. The price of bread doubled on Monday, the banks are running out of money because there is no paper to print it on, and corpses are piling up because crematoriums have no gas.

Mr Bush has astutely offered lots of aid for a post-Mugabe Zimbabwe, in the hope of encouraging

moderates within the ruling party, ZANU-PF, to nudge the old man out. But he is not planning any tougher action, because he says it would be wrong to “second guess” South Africa, Zimbabwe's most important neighbour. South Africa's president, Thabo Mbeki, dares not risk a public confrontation with Mr Mugabe; he fears a row with his African allies, some of whom think Mr Mugabe is a nationalist hero. Standing beside Mr Bush on a lawn in Pretoria, Mr Mbeki repeated his old mantra that Zimbabweans must sort out their own mess. He added, quite falsely, that ZANU and the opposition were in negotiations. Meanwhile, the police arrested the mayor of Harare, an opposition party member, for the crime of going to his office and trying to work.

Mr Bush was hoping to spend most of his trip discussing less problematic countries than Liberia and Zimbabwe. He talked of earmarking $10 billion of aid for African countries that battle corruption and promote democracy. His aim, Mr Bush said, was to “support the leaders who accept the principle of reform”.

On the sunnier side

In South Africa, which is too wealthy to need much aid, Mr Bush spoke more about trade. On July 9th, he toured a Ford car factory near Pretoria. Alec Erwin, South Africa's trade minister, says that Ford could soon start exporting cars made in South Africa to America. It would thus join other carmakers which are already taking advantage of the country's good infrastructure and relatively cheap labour. America's relations with South Africa are generally constructive, and talks to set up a United States-Southern Africa free-trade area are under way.

Mr Bush and Mr Mbeki even managed a show of unity on the subject of AIDS, about which Mr Mbeki holds some odd views. Both presidents said that, although talks had only just begun about how to spend the putative $15 billion Mr Bush recently promised to fight the disease, it would be necessary to make treatment (that is, drugs) available to more people.

That might prove a bone of contention between the two countries later this year, at the world trade talks in Doha. Mr Mbeki wants the American government to be more forgiving of poor countries that violate drug patents, most of which are held by western firms. Brand-name drugs to combat AIDS (among other diseases) remain too pricey for millions of HIV-infected Africans. Mr Mbeki argues that laxer intellectual-property rules would make them cheaper. Yet his own government has failed to take full advantage of deep discounts offered by drug firms.

As Mr Bush spoke optimistically about Africa's future, the UN Development Programme (UNDP) released its annual “Human Development Report” (see article), to air gloomier data. The UNDP ranks countries by their levels of poverty, illiteracy, unemployment and life expectancy. Of the 21 countries where life grew harder in the 1990s, two-thirds were African.

The main reason is that AIDS is causing Africans to die younger—in some countries dramatically so. In Zimbabwe, for example, life expectancy has crashed from 56 years in the early 1970s to 33 today. The good news is that, on current trends, Africa will meet some of the UNDP's “development goals”, such as achieving universal primary education and halving the proportion of its people who live in extreme poverty. The bad news is, it will not do so until 2129 and 2147 respectively.

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Algeria's Islamist leaders

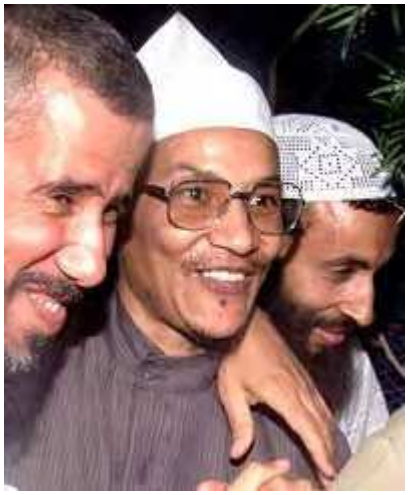
Still shackled

Jul 10th 2003
From The Economist print edition

Abassi Madani and Ali Belhadj have served their terms but are not free

Reuters

Get article background



Will Ali Belhadj stay mum?

MANY prophesied that they would never be released. The leaders of Algeria's outlawed Islamic Salvation Front (FIS), detained since 1991, have been so demonised that it was hard to believe they would ever be let out of jail. But on July 2nd, when they had served their 12-year sentences to the very last day, Abassi Madani, and his deputy, Ali Belhadj, were quietly set free.

The two Islamists once led the most popular political party in Algeria. They were arrested during a turbulent summer of protest in 1991. A few months later, the FIS convincingly won the first round of parliamentary elections. The Algerian army then intervened, scrapping the election and outlawing the party. In this way, the army set off an armed insurrection by groups of Islamic radicals that has yet to be totally extinguished.

Controlling political power from the shadows, Algeria's military rulers have spent the past 12 years doing all they can to obliterate all memory of the FIS. Successive elections, mainly rigged, have endowed the country with a democratic façade that barely disguises army rule. Throughout most of that time, the army battled against militant Islamists, causing Algerians to suffer horribly from the brutalities of both sides.

So how much of a threat to the regime are the newly freed leaders? Judging by the crippling restrictions the authorities slapped on the two men, they still do not believe the Islamists to be a spent force. Barely were the two out before it was announced that they would not be allowed to vote, stand in elections, support candidates, speak at public or private meetings, have any involvement with civil associations or charities, or pursue any religious, political or cultural activities. Indeed so determined are the authorities to keep the FIS leaders in a box, that they expelled the foreign correspondents who came to cover their release.

The FIS is in no position to reconstitute itself as a party. Still illegal, it is also in disarray; its own armed wing surrendered two years ago in exchange for a government amnesty. Many of its former supporters, traumatised by the violence of the past decade, may well have lost their enthusiasm. But the FIS was not just an ordinary party; it was also a *sentiment*, as a supporter once eloquently put it.

Part of its appeal was its claim to have God on its side. But it was populist too, promising a new and just order to a predominantly young population, which could see only a bleak future. And now, in 2003, Algeria is bedevilled by much the same problems as it was in 1991: corrupt and arbitrary government, high unemployment, a housing shortage and what Algerians call *hogra* (social and political exclusion).

Of the two freed men, Algeria's military-backed rulers are much more wary of what Mr Belhadj may do. Unlike the elderly Sheikh Madani, Mr Belhadj, who is 47, may well harbour ambitions of a political comeback. A charismatic, fiery preacher, he stayed defiant throughout his prison years. His first act on release was to go to the television building in Algiers, where he was arrested in 1991 as he was about to reply to some allegations against him. He is said to have demanded from astounded employees the right of reply that was denied him by his arrest.

Supporters of the two leaders suggest that they may seek to launch a peace initiative to get the

country's remaining Islamic militants to lay down their arms. But, if this is their plan, it is far from certain that the army will allow them the role. Their release comes as Algeria is going through yet another period of political flux. Presidential elections are due next year, and there are mounting signs that the army is no longer prepared to back the incumbent, Abdelaziz Bouteflika. So far, his only declared rival is Ali Benflis, the prime minister he sacked earlier this year. Mr Benflis has been consolidating his hold over the National Liberation Front (FLN), the majority party of which he is secretary-general.

There is likely to be fierce jostling between the two men. Mr Bouteflika, who throughout his presidency has fought for power against the officers to whom he owes his position, recently changed tack and started flattering the army. It is not yet clear if other candidates will enter the fray, or what kind of outcome the army factions will allow. What is certain, however, is that the army commanders do not want the FIS leaders to play any part. That is the message of the restrictions.

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South African census

Who are we?

Jul 10th 2003 | PRETORIA
From The Economist print edition

Blacker, slightly richer and more numerous

FIFTEEN officials died counting South Africans in the census taken in October 2001, at least four of them from gunshot wounds. Many also had to face the dogs and electric fences of white residents unwilling to answer questions. The violence and the fear help explain the census results, published this week. These suggest that the white population is shrinking fast as a share of the total: from 10.9% in 1996 to 9.6% two years ago. The numbers speaking Afrikaans or English as a first language are also sharply down. English is now only the fifth most popular language.

Statisticians say that real emigration since 1996 is much higher than the official rates. Judging by immigration reports from Australia, Canada, America, New Zealand and Britain, more than 1m white South Africans (out of about 5m) left the country in the past few years.

The census also shows that 41.6% of adult South Africans lacked formal work in 2001, a rate much higher than the official figure of about 30% and sharply worse than it was in 1996. Among blacks, one in two lacked a job.

But, in other ways, many things have improved under democratic rule. On average, South Africans are better educated, slightly richer, and better housed, lit and heated than they were in 1996, though the averages hide persistent inequality. People also have more telephones, fridges, radios, computers and cars. They also have more neighbours. The overall population rose from 40.5m to 44.8m in 2001, up 10%.

Some of that rise is explained by migrants from nearby countries such as Zimbabwe. And the true total would probably be much higher if all illegal immigrants were included in the census. But counting people who squat in rough spots such as Johannesburg's Hillbrow is even more dangerous than braving the rottweilers of the white suburbs.

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Local democracy in Iraq

Tiny steps in the dance

Jul 10th 2003 | BAGHDAD
From The Economist print edition

The new council will not dilute American rule but it is a start of sorts

AP

So do something about this, the councillors will be told

Get article background

FOR most Baghdadis, July 7th was just another stifling summer day, though perhaps a bit tenser than most after the killing of three American soldiers in the capital in the preceding 24 hours, and the broadcast of a taped address by Saddam Hussein over the weekend. But for Paul Bremer, head of the Coalition Provisional Authority (CPA), it was “probably the most important day since April 9th, when the coalition came and liberated you from the dictatorship of Saddam Hussein.” The inauguration of the capital's 37-member municipal council, which Mr Bremer was addressing, marked the “resumption of the democratic system in Baghdad”, and was, he said, a step towards the establishment of an elected national government.

Well, up to a point. For the past six weeks, the CPA has been supervising the creation of a system of advisory councils throughout the country. In Baghdad, local caucuses chose 88 neighbourhood councils, which in turn chose nine district councils, which in turn chose the city council.

American officials freely admit that the improvised selection process fell far short of the democratic ideal. They had the final say on who made the cut, juggling the results to make sure they matched up with their vision of what should constitute a cross-section of the community. “Maybe one guy had 50 votes, the other guy had 30, but [we chose] the guy with 30 based on other criteria,” said P.J. Dermer, a member of the CPA's governance department.

The advisory councils have been involved in projects that range from street-cleaning to recruiting volunteers for an Iraqi security force. However, they have no budget—though they are allowed to request funds from the CPA—and they have no executive powers. In terms of form and function, they are less like American democratic institutions, about which Iraqis have been hearing so much, than the powerless city councils of other Arab one-party states, which primarily serve as intermediaries between the public and an all-powerful centralised regime.

If the councils' main job is liaison, as one CPA official suggested, they have their work cut out. Baghdadis complain endlessly about the chaos into which their capital has been thrown, particularly by the lack of electricity for more than a few hours every day. The CPA admits that it cannot get the lights back on, but wants the public to be told why.

The American explanation is that Saddam Hussein made the capital dependent on imported electricity, and that thieves are tearing down the power lines for copper. But two young men running a corner shop in northern Baghdad are uncertain whether they want to believe this explanation, or the more sinister one suggested by a notice on an American tank, which they claim a friend of theirs saw with his own eyes: “You give us security, and we'll give you power and water.”

Though drawn to rumours of a blackmailing tank, few residents of this particular neighbourhood seem to have much sympathy for the Iraqi fighters taking pot-shots at American soldiers: there is not much point, they suggest, in launching an insurgency if what you want is stable government. But they have lost trust in the American authorities, and most call for an Iraqi government to be established.

Shias, but which Shias?

Mr Bremer is expected soon to give the names of the 25-30 members of a national “governing” council (as opposed to the “advisory” council he originally espoused). Iraqi opposition groups, which had previously attacked the national council as democratic window-dressing, now embrace it, claiming that Mr Bremer has promised them real executive powers. However, the council will still be appointed by the Americans. And although CPA officials say that they intend it to reflect the country's sectarian balance—which means that a majority of the members will be Shia—there will be strong complaints if it excludes popular but radical groups, such as the Sadr movement.

The CPA claims that this transitional process will help to acquaint Iraqis with the democratic process. Time is required to reassemble electoral rolls and establish a secure environment for voting, let alone for the contentious task of drafting a constitution. But the passage of time will also cement the authority of the American-screened council members in their communities, giving them an edge when Iraqis do eventually compete in elections.

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Iran's nuclear programme

Enriching

Jul 10th 2003
From The Economist print edition

The questions about Iran's nuclear past

A FIRST report, last month, by the International Atomic Energy Agency (IAEA), the UN's nuclear watchdog, expressed “concern” at a string of previously undeclared nuclear activities in Iran. A second damning report, when the agency's board meets in September, could raise a storm. So on July 9th Mohamed ElBaradei, the IAEA's director-general, was in Tehran hoping to find answers to the questions in his June report, and to win Iran's acceptance of toughened safeguards.

A team of experts will go to Iran next week, he said, to explain how more rigorous inspections could help dispel doubts about its nuclear ambitions. But those are multiplying. In a week when Iran confirmed it had completed tests of its 1,300km-range Shahab-3 missile, evidence was accumulating that seemed to undermine the claim that its nuclear activities are entirely peaceful.

Mr ElBaradei wants to know why Iran produced uranium metal, not needed for its planned nuclear reactors, but handy for making bombs. And why build a heavy-water research reactor, ideal for making bomb-usable plutonium, when Iran's energy plans depend on light-water reactors? But the IAEA has been keenest to probe Iran's claim that it is building a sophisticated uranium-enrichment plant at Natanz—a pilot plant and a much larger production-scale plant—without ever having done tests with uranium gas to prove its centrifuge machines work. These can produce low-enriched uranium for reactor fuel, or highly enriched uranium for a bomb. Iran is obliged to report either sort of work, but denies flatly it has done any.

Iran shrugged off the agency's June report, which detailed its undeclared import in 1991 of 1.8 tonnes of natural uranium (from China, although the IAEA does not say so), claiming that its safeguards agreement did not require it to do so. When some of this material was found to be missing—1.9kg of uranium hexafluoride—Iran blamed leaky cylinder valves. Was it used instead for testing centrifuges?

Inspectors have been keen to explore the Kalaye Electric Company in Tehran, where some centrifuge parts were made. They have visited part of the site, which was recently refurbished, but were not allowed to take samples to check for illicit enrichment activity. An Iranian opposition group that first alerted the world to the existence of the Natanz plant has accused Iran of secretly enriching uranium at other sites too. This week it claimed that nuclear activities were under way at a military complex north-west of Tehran.

Without access, the IAEA cannot judge the merit of such charges. The Iranian government has allowed some sampling at the Natanz pilot plant. The agency refuses to comment on its findings, saying its work will be ready for the September board meeting. Others familiar with the highly sophisticated analytical techniques now available believe the evidence shows that Iran has done undeclared uranium work of some sort at Natanz. The agency has urged Iran not to start up the pilot plant, as that would mask any past activity.

Uranium enrichment is hard to detect without knowing where to look. If Iran is shown to have cheated on its safeguards agreement, not even toughened safeguards will then be taken as sufficient reassurance that all such cheating had stopped. Privately some European officials have been pressing Iran to abandon all aspects of the nuclear fuel business. Caught uncomfortably in the IAEA's searchlight, Iran is pondering its options.

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Palestinians in Iraq

Back in a tent

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The Palestinians were seen as Saddam's supporters and are suffering for it

AFP

Indirect victim of the Iraqi war

AT TWO months old, Rasmia Mahmoud was swept in an Iraqi Jeep from her home in Haifa to a tent in Iraq. Now, 55 years later, she is back under canvas, sharing a sun-baked football pitch with some 2,500 Palestinians evicted by Shia mobs from their Iraqi homes. They chased her and her grandchildren out at gunpoint, she says, after threatening to burn their lodgings.

Until the fall of Baghdad, there were 35,000 Palestinians in Iraq, many of them living in government-subsidised housing. Now they are dispersed in tents, either in the outskirts of Baghdad or in a stony Jordanian refugee camp 500km (300 miles) to the west, plum in the heart of the desert.

And still they keep coming. Their eviction, says Human Rights Watch, was encouraged by Shia landlords, angered by decades of favouritism to Palestinians, not least in their frozen rents. When Saddam Hussein appropriated buildings for Palestinian refugees, the 1,300 dinar annual rent was worth about $3,000. Now it is worth less than a dollar. Landlords who tried to challenge the agreements in court lost their case.

But rent was only part of it. Shias saw Palestinians as Saddam's Sunni partisans, filling the ranks of his intelligence services and *fedayeen*. Stricken by sanctions and an ideology of Arab nationalism that subsumed Iraq into a Sunni-dominated Arab world, Iraq's Shia majority resented the largesse that the Baath Party diverted to Gaza.

Yet many Palestinians, too, had a difficult life under the Baath. Iraq, alone among the Arab states, barred the UN from supervising its Palestinian refugees, and imposed a welter of restrictions, in the name of keeping alive their desire to return to Palestine. In order to circumvent bans on owning a car, a house or a bank account, Palestinians had no choice but to join the Baath Party.

Many of them looked up to Saddam Hussein as the only Arab head of state in a generation to fire missiles at Israel. Now their fate reflects his.

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Russia

Power struggle in the Kremlin

Jul 10th 2003 | MOSCOW
From The Economist print edition

When an election result is all-but-guaranteed, what's left to fight for? In Russia, there's still a great deal

Get article background

TWO explosions, one real and the other political, have kicked off Russia's election season. The real one, a suicide-bomb attack by Chechen rebels at a rock concert in Moscow on July 5th (see article), killed at least 16 people. A wave of such attacks in the run-up to next March's presidential election will remind Russians of Vladimir Putin's failure to end the conflict in the breakaway republic, nearly four years after they elected him on his promise to do so.

The political bomb, the arrest of a top businessman, was probably a bigger shock to foreign investors than to ordinary Russians. It too marks the start of an electoral campaign. But the campaign is not for the elections themselves: both Mr Putin's victory, and a majority for pro-Kremlin forces in the Duma (parliament's lower house) this December, seem assured. Rather this is a contest for the second tier of power: the job of managing the election campaigns for the Kremlin. The prize is influence in the next Duma and government, and thence on the presidential succession.

Platon Lebedev, a key shareholder in Yukos, Russia's biggest oil producer, was arrested on July 2nd, accused of illegally acquiring shares in a fertiliser company in 1994. In a country where powerful people are arrested only if they annoy someone more powerful, that seemed to break a pact that Mr Putin and the country's top businessmen had reached in 2000: that he would overlook any ill-gotten gains they might have made during the reckless privatisations of the 1990s, if they now stayed clean and out of politics. It was universally taken as a sign from the Kremlin that Mikhail Khodorkovsky, Yukos's boss, had overstepped the line by openly financing two political parties—the Union of Right Forces and Yabloko—while associates of his, he admitted, gave to the Communists.

Yet Mr Khodorkovsky thinks that if Mr Putin, who turfed two meddlesome magnates out of Russia early in his term, is annoyed with him, that was not the main reason for the arrest. Yukos, he said a couple of days later on television, “is the country's biggest company, and its most independent. That, we understand, is unpleasant, especially to people who think in the old style.” Such people, he hinted, are among those close to Mr Putin, and Mr Lebedev's arrest was “the start of a struggle for power which will have to be concluded after the [presidential] elections in March.”

The tensions in Mr Putin's circle have existed since his predecessor, Boris Yeltsin, plucked him from relative obscurity to become briefly prime minister and then acting president, before he was elected head of state. In an attempt to restore order and shake off Mr Yeltsin's influence, Mr Putin surrounded himself with trusted people, many of them “Chekists”, like him, from the security services. Russia's top businessmen, on the other hand, have closer links with the remnants of Mr Yeltsin's team, who ran the country when they got rich. Both groups must already be thinking about who will replace Mr Putin in 2008.

The players line up

Party	Profile	Leader
Those who usually support the Kremlin		
United Russia Coalition		Four-man council comprising:
Unity	Original pro-Kremlin party	Sergei Shoigu, emergency situations minister;
Regions of Russia	Hotch-potch of governors' representatives	Mintimer Shamiev, Tartarstan president;
Fatherland-All Russia	Businessmen and ex-Communist wheeler-dealers, loyal to Vladimir Putin	Yuri Luzhkov, Moscow mayor; Boris Gryzlov, interior minister
People's Deputy	Security-service types, were part of United Russia; appeals to leftists	Gennady Raikov
Liberal Democrats	Illiberal and undemocratic	Vladimir Zhirinovsky
Those who sometimes don't support the Kremlin		
Communists	Still has best grass-roots network, but supporters are dying off	Gennady Zyuganov
Agroindustrial group	In effect, a branch of the Communists	Nikolai Kharitonov
Union of Right Forces	Free-marketeers first, promoters of liberal values second	Boris Nemtsov
Yabloko	Liberal-values promoters first, free-marketeers second	Grigory Yavlinsky

Source: *The Economist*

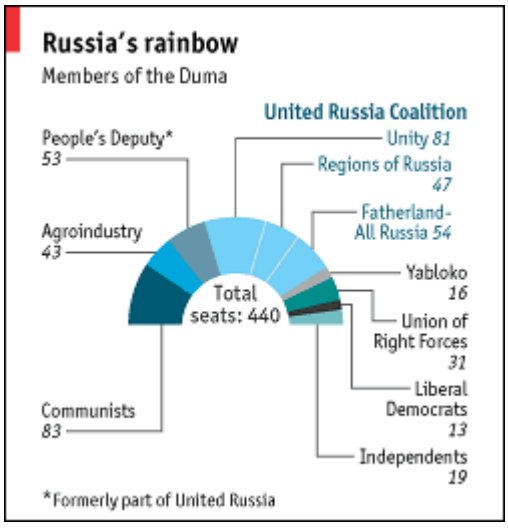
Bashing big businessmen is popular with ordinary Russians and could make the St Petersburgers look like smart electioneers. It would also weaken Mr Khodorkovsky, a multiple threat to them. Not only for his own ambitions—he has often said he will resign in 2007, without explaining what he would do next—nor because, by financing other parties, he threatens the pro-Kremlin majority, but also because Yukos's planned merger with Sibneft, another oil firm, will make his company so big as to be nearly untouchable.

Purely by chance?

It was surely no coincidence that after Mr Lebedev's arrest, Russia's antitrust commission said it would delay approval of the merger for another three weeks. Then the country's chief prosecutor said that Yukos's tax position would be examined. And a few days before, Rosneft, a state-owned oil firm whose boss and Mr Khodorkovsky were already at loggerheads, accused Yukos of illegally getting shares in one of its subsidiaries—though that, say both companies, is indeed a coincidence.

Mr Khodorkovsky has no doubt trodden on some toes in his career and may do so again, and his woes may be a settling of personal scores as much as anything. But they are a clear sign to other plutocrats. Just days before Mr Lebedev's arrest, another of them, Vladimir Potanin of the Interros group, made a public show of contrition for past excesses and of fealty to United Russia, the coalition in the Duma that backs the Kremlin.

So will the St Petersburgers win out? They are indeed strong. Under Mr Putin several government agencies, such as the narcotics squad and the wiretap service, have been brought back inside the fold of the Federal Security Service (FSB). This week, in the wake of the Moscow bombing, mobile-phone firms agreed to remove the scrambling on their systems to let the FSB listen in on calls. Top St Petersburgers include Igor Sechin, the deputy head of the presidential administration (who controls access to the president); Sergei Ivanov, the defence minister; and Boris Gryzlov, the interior minister. One of United Russia's leaders, Mr Gryzlov himself recently launched a vigorous pre-electoral campaign with a wave of high-profile arrests of non-political villains.



But they have opponents. The People's Deputy party, a component of United Russia dominated by Chekists, announced this month that it was breaking off, to run in the elections alone. This, says Nikolai Petrov at the Carnegie Endowment in Moscow, may be a sign that it failed to get control of the pro-Kremlin party. And wise heads may be counselling Mr Putin

that such blatant manipulation of the legal system in a private or political feud looks bad for the country and has to be stopped.

At least, that is what Mr Khodorkovsky would like to think. Most intriguingly, Mikhail Kasyanov, the prime minister and a member of Mr Yeltsin's clan, is the most recent bigwig to have weighed in, describing Mr Lebedev's arrest as “excessive”.

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Chechen suicide bombers

The black widows' revenge

Jul 10th 2003 | MOSCOW
From The Economist print edition

Russians will have to get used to living with terrorism on their doorstep

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“GO AWAY,” the young woman told a policeman trying to question her as she lay dying amid the remains of her partly exploded bomb. “I couldn't...I will not get to Allah.” Soon, she did.

The first Chechen suicide bomber—also a woman—blew herself and a Russian army truck up three years ago. But it has become one of the methods of choice since last autumn, when a band of rebels took a Moscow theatre and its audience hostage and threatened to blow up everyone, themselves included. (They and 129 hostages were killed by the subsequent rescue.) The most devastating suicide bomb attack, last December, destroyed the government headquarters in Grozny, the Chechen capital, and killed around 80 people. In the last two months there have been at least four more, all aimed at military targets in or near Chechnya, claiming over 100 lives. Some, like the double bombing at a rock concert in Moscow last weekend that killed at least 16, were carried out by women. On July 9th a Chechen woman was caught taking a bomb into a Moscow restaurant.

“It's completely alien to our culture,” rails an indignant Jabrail Gakayev, a Chechen historian at the Russian Academy of Sciences. Even during Russia's protracted war against the Chechens and their Caucasian neighbours two centuries ago, he says, “women only took up arms when the men were killed and they had to protect their children.”

That, in a way, is what is happening. Young Chechen men are the Russian army's favourite target for arrest, torture and disappearance. Muslim fundamentalists who have joined the Chechen rebels are targeting women who have lost husbands and brothers, and are willing to kill themselves in revenge. Russian officials speak of training camps for “black widows”. However, says Shamil Beno, a Chechen foreign minister during the republic's brief, self-proclaimed independence in the 1990s, “I don't think they do it for religious-fanatical reasons, but for practical ones: there's nothing else they can do against the army. If there's no change in direction in the next few years, we think there are 30,000 families that could produce *shahids* [martyrs], families that have suffered terribly and see no alternative.”

The Russian government has been trying to “normalise” Chechnya. A suspiciously well-attended referendum on a new constitution was held last March, and presidential elections are due on October 5th, with a promise that the republic will be granted some sort of autonomy. Last month an amnesty for participants in the conflict was declared. But its terms would exclude many rebels and seem more designed to pardon Russian troops, while the election will most likely be a way to legitimise a pro-Moscow puppet. And the Chechen rebels now know that Moscow is wide open to suicide attacks.

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A referendum in Corsica

A worrying result

Jul 10th 2003 | PARIS
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The rejection of a French plan for Corsica could prompt more violence

AP

HE WAS regarded as the man with the magic touch. The government needed help calming its striking teachers? Bring in Nicolas Sarkozy, the high-flying young interior minister. The Corsican question needed attention? Dispatch “Super Sarko”. Yet this week, despite his many visits to the island to drum up a yes vote, Corsicans rejected the offer of limited autonomy from mainland France (albeit by a margin of only 2%), so dealing Mr Sarkozy his first big political setback.

His approach was always going to be risky. President Jacques Chirac studiously kept above the debate, urging Corsicans only recently to vote yes. Mr Sarkozy, by contrast, not only campaigned hard but could scarcely conceal his delight when, two days before the vote, the police arrested Yvan Colonna, France's most wanted man, who had been in hiding in a shepherd's hut on the island.

A Corsican separatist, Mr Colonna was wanted in connection with the assassination in 1998 of Claude Erignac, the former prefect of Corsica (in effect, its governor). At last, it appeared, the state was clamping down on the political violence that for decades has plagued this island, part of France since 1768. But, if the arrest was stage-managed, the plan backfired. “Undeniably,” said Mr Sarkozy after the no vote was announced, “it's a disappointment.”

The high-profile interior minister will doubtless recover. He is juggling other more popular matters, from tightening security to curbing immigration. More seriously for the island, however, is where this defeat leaves the separatists.

The answer is muddled because the referendum was. Voters were being told by separatist parties such as Corsica Nazione that a yes vote would be a welcome step towards autonomy, while at the same time Mr Chirac was saying that by voting yes the islanders would be “affirming their attachment to France”. While the proposal to merge the island's three elected bodies into one would indeed have brought a bit more autonomy—over matters such as the environment and tourism—it was also an effort by the government to thin down Corsica's bloated bureaucracy and boost private investment. The no vote, in short, was not a clear-cut rejection of the nationalist cause.

All the same, the nationalists are bruised. The worry now is that the militant fringe will step up the violence. There is frustration at the failure of negotiations to lead anywhere, and resentment at the arrest of Mr Colonna, which some see as a sign of the return of a policy of repression. Since autonomy talks began in 1999, when there were 338 explosions on the island, violence had declined a bit: to 250 blasts in 2002, and 134 in the first half of 2003.

Already, however, on the night of the vote, four French-owned second homes were bombed. Opinion polls consistently show that only a tiny minority of Corsicans want independence from France. But the referendum proposal's failure could re-ignite the separatist cause.

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A German scandal

An underlying theme?

Jul 10th 2003 | BERLIN
From The Economist print edition

The downfall of a leading Jewish German sets off awkward vibrations

GERMANS often complain that they don't have the juicy high-level scandals that the British, French and Americans seem to lap up. But now they do have one. It has orgies, drugs, politicians, television celebrities, prostitute-smuggling rings, suicide, phone taps, code names—the lot.

Instead of revelling in it, however, many Germans seem embarrassed. For the plot's main character so far is Jewish, and happens to be vice-president of Germany's Central Committee of Jews, president of the European Jewish Congress, and the son—by the by—of Polish Jews saved from the Holocaust by Oskar Schindler, later of film fame. Most Germans are still wary of giving the faintest impression they might pillory someone because he is Jewish.

The original case against Michel Friedman, a lawyer and acerbic television chat-show host, had nothing to do with his Jewishness. His name was simply one of a dozen or so, said to include those of leading politicians and diplomats, that happened to crop up during police investigations into an international sex ring which involved smuggling young women out of Poland and Ukraine and forcing them into prostitution in Germany. Two women apparently accused Mr Friedman of having sniffed cocaine and of having an orgy with them in a smart Berlin hotel. Police later searched his home and found traces of the drug.

Mr Friedman's friends maintained that the way he was singled out and hounded by the press had everything to do with his being Jewish. The whole affair, they said, was a symptom of the underlying anti-Semitism that still bedevils German-Jewish relations. And it was surely not by chance that the scandal was first leaked just a few days after the death of Jürgen Möllemann, a leading liberal politician, in a parachute fall.

Mr Möllemann, who is widely believed to have committed suicide, had once accused Mr Friedman of fostering anti-Semitism because of his “intolerant and spiteful manner”, and had published a pamphlet attacking his “pro-Israeli” views in last year's general election campaign.

This week, Mr Friedman admitted possessing cocaine and agreed to pay a fine of *euro*17,400 ($19,700) in return for all further legal proceedings against him being dropped, so avoiding an embarrassing court hearing. He also resigned from all his public offices.

Was such a hullabaloo really warranted? Certainly, there was quite a bit of *Schadenfreude* in the popular reaction to the affair. Most Germans think Mr Friedman is unduly aggressive, arrogant and moralistic. So they enjoyed seeing him get his come-uppance. A touch of anti-Semitism may be discernible here and there. But on the whole the German press has treated him more gently than they would have any other equally prominent person caught up in so colourful a scandal.

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Turkey and the United States

A partnership at risk?

Jul 10th 2003 | ANKARA
From The Economist print edition

The strategic interests of America and Turkey may be diverging dangerously

THE much-vaunted “strategic partnership” cemented during more than half a century between Turkey and the United States looked in danger of coming unstuck four months ago when Turkey's parliament refused to let American troops use eastern Turkey as a launch-pad from which to attack Iraq. Since then, the two countries have tried to patch things up. But a new row has made matters worse, all over again. Turkey's top general, Hilmi Ozkok, said that the latest quarrel, sparked by the arrest on July 4th of 11 members of Turkey's special forces by American troops in northern Iraq, marked the “biggest crisis” ever between the armed forces of the two NATO allies. For now, the strategic-partnership phrase has dropped out of sight.

The captured Turks (freed a couple of days later) were members of a force deployed in the Kurdish enclave since 1996 to monitor a ceasefire between the two main Kurdish factions running northern Iraq. The Americans say they arrested the Turlish soldiers on suspicion of involvement in a plot to kill the Kurdish governor of Iraq's oil-rich province of Kirkuk. The Turkish special forces were further said to be acting in cahoots with an ethnic-Turkish militia called the Turcomen Front, which has been covertly armed and trained by Turkey as a lever against the Iraqi Kurds.

The American claims of a murder plot were nonsense, said Turkey's foreign minister, Abdullah Gul. Deniz Baykal, leader of the Republican People's Party, parliament's main opposition, fumed that nothing short of a formal American apology would do. Hursit Tolon, a top general, called the incident “disgusting” and cancelled a trip to America.

The captured Turks said that American soldiers had hit, handcuffed and cursed them, putting sacks over their heads during two days of interrogation in Baghdad. Anti-American feeling among Turks at large is rising. It could turn nastier if Congress passes a resolution recognising the deaths of at least 1m Armenians in Turkey in 1915 as genocide.

The American government insists that the recently captured Turks were not so innocent. Explosives and other apparently incriminating evidence were said to have been found on them. But even if that were so, the Turks think the Americans should have dealt with the matter through diplomatic channels rather than treat the Turkish soldiers as if they were enemies. Diplomats in the American State Department may well share that view. They had apparently been kept in the dark by the Pentagon.

The prevailing suspicion among ordinary Turks and their leaders is that hawks in the American administration are out to punish them for not letting American troops use Turkey as a rear base in the war against Iraq. But there is a deeper explanation. The two countries' interests have been diverging since the cold war ended. Though it backed the Americans strongly in the first Gulf war, in 1991, Turkey has since bitterly regretted one outcome: the consolidation of Kurdish self-rule in northern Iraq. Not only did it fan separatist feeling among Turkey's own Kurds; the war's outcome also lost Turkey trade with Iraq worth billions of dollars—a loss that Turks think was never appreciated by the Americans. Nor was Turkey compensated.

The Turks are becoming no less glum about the outcome of the recent American war, for Turkey is being slowly but surely eased out of northern Iraq, once again to the great satisfaction of Iraq's Kurds. The spectre of a Kurdish renaissance, courtesy of the Americans, is jangling Turkish nerves. That, not just the recent spat over the 11 captured Turkish soldiers, is what truly irks the Turks.

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Greece's government

A big clean-up is promised

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The prime minister, Costas Simitis, is tackling corruption in his own party

Reuters

Simitis gets out his broom

FLUSHED with self-confidence after Greece's competent six-month stint in the EU presidency, Costas Simitis, the prime minister, has decided it is time to clean up the governing Pan-Hellenic Socialist Movement (known as Pasok) and make it more “European”. With a bright new social-democratic image, the party just might win next April's election, so ensuring that Mr Simitis is the one to welcome the world's sporting elite to next summer's Olympic games in Athens.

His first move was to sack Costas Laliotis, Pasok's secretary-general and a symbol of its outdated populist ways. Mr Laliotis was unpopular with many Greeks because of his cosiness with a group of local building contractors (he served a long stretch as public-works minister) and his diehard anti-Americanism. During the war in Iraq he encouraged the teachers' union to stay off work and take primary-school pupils to shout “American murderers” at demonstrations.

Michalis Chrysohoidis, one of the prime minister's modernising faction, has taken Mr Laliotis's job. As public order minister, he took credit, together with Scotland Yard and the FBI, for the arrest last year of some 20 members of a left-wing terrorist group called November 17, whose victims included one British and several American and Turkish diplomats.

Mr Chrysohoidis will still have his work cut out to persuade voters that Pasok is abandoning its knee-jerk nationalism and its deeply entrenched system of patronage. Party strongmen control most public-sector appointments, from university professors and hospital directors to local government officials and even football referees. Businessmen who deal with state enterprises say corruption is still rife.

In opinion polls Pasok trails New Democracy, the centre-right opposition, by some nine percentage points. But Mr Simitis is still the party's biggest asset. His popularity, though well below its peak three years ago when he steered Greece into the eurozone, is not far behind that of Costas Karamanlis, New Democracy's leader.

To win back the middle-of-the-road voters who decide Greek elections, Mr Simitis is to launch a “social convergence charter” underlining, among other things, his intention to reduce unemployment and make the civil service more honest and efficient—two top priorities for voters.

This week Mr Simitis announced that Pasok's MPs could no longer hold shares in offshore companies, a favourite tax dodge for the politically connected. The Athens stock-exchange watchdog will also scrutinise MPs' brokerage accounts, a measure meant to remove a popular perception that influential Pasok people manipulated the bourse in the boom that preceded Greece's entry into the eurozone.

Has Mr Simitis done enough to reassure Greeks that Pasok is truly changing its ways? Only if he can deliver results. One minister, Stefanos Manikas, was sacked last month over the stock-market scandal. But more resignations (and prosecutions too) will be needed to persuade voters that a clean-up is really under way.

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Charlemagne

Burlesquoni

Jul 10th 2003
From The Economist print edition

Behind Silvio Berlusconi's antics, has Italy's attitude to the European Union changed more deeply?

STRANGE as it may seem, there was a time when European federalists looked keenly forward to Italy's presidency of the European Union. The Italians have traditionally been among the most ardent promoters of European unity. The EU traces its origins to the Treaty of Rome in 1957. And it was during an Italian presidency in 1990 that Margaret Thatcher was cornered at a summit and forced to agree to the negotiations that led to the Maastricht treaty and thence to the creation of a European currency and foreign policy. From the federalist viewpoint, another Italian presidency looked ideal for the final stage of negotiations, starting in October, to clinch a European constitution.

But the federalists had not counted on Silvio Berlusconi. Rather than start the Italian presidency with a renewed drive towards European unity, Mr Berlusconi sparked a row with Germany that is still smouldering. His comparison of a hostile German MEP to a Nazi concentration-camp guard was incendiary enough; his half-apology failed to dampen things down; and then Stefano Stefani, a junior minister, re-ignited the flames by accusing German tourists of being “stereotyped blondes with ultra-nationalist attitudes” and of aggressive behaviour on Italian beaches. To display his annoyance, Chancellor Gerhard Schröder this week cancelled his Italian summer holiday.

All very elevated, no doubt. But Mr Berlusconi's threat to the European dream goes well beyond his remarkable lack of diplomacy or even the alleged threat he poses to Italian democracy through his power over the media and his war with the judiciary. He has also changed his country's traditional European policy. While his predecessors stressed the goal of ever closer political union, especially among the EU's original members, Mr Berlusconi has championed the idea of enlarging the club, suggesting that even Russia and Israel might one day join it—a notion that the ever-closer-union crowd regard either as crazy or as deliberate sabotage. He has insisted that Italy will be more assertive in fighting its corner in the EU, provoking a series of rows over issues like fines on Italian farmers and the siting of a European food agency. Senior ministers in his government have even cast doubt on whether the single currency will survive.

Perhaps most important, Mr Berlusconi seems more instinctively drawn to the United States than to Italy's time-honoured European partners, France and Germany. In the run-up to the Iraq war, he was one of eight European leaders who, along with the British, Spaniards and a clutch of central Europeans, signed a letter backing the United States. Partly as a result, he has poisonous relations with the German and French leaders and gets on famously with George Bush.

These changes in Italian foreign policy have coloured European reaction to the great Berlusconi gaffe. Much of Europe's left seems to regard the Italian leader's pro-Americanism as inseparable from his alleged corruption. By contrast, Britain's Eurosceptic right is sorely tempted to ignore all those unsavoury allegations (“Aren't all Italians like that?”) and to embrace the Italian prime minister as one of their own. Neither side, however, seems to have worked out whether the changes in Italy's European policy are simply a quirk of Mr Berlusconi's personality or instead signify something more profound.

The Italian left is inclined to dismiss the Berlusconi policy on Europe as governed by the same instincts as his domestic policy. “Europe is a place where laws come from”, says one politician, “and he doesn't like laws.” It is certainly true that one EU policy that has the Italian leader particularly agitated is the effort to set up a pan-European arrest warrant to deal with cross-border crimes, including corruption. Mr Berlusconi has warned his European colleagues that such a scheme would encourage “red judges” to pursue political vendettas; one of his ministers speculated recently that one of the first targets of a European prosecutor might be Mr Berlusconi's own business empire.

But whatever Mr Berlusconi's motives, there has also been a genuine ideological shift by parts of the Italian right. The Northern League, junior partners in the ruling coalition, are now strongly anti-European as well as anti-immigrant. Some senior ministers in Mr Berlusconi's team, like Giulio Tremonti, the finance minister, and Antonio Martino, the defence minister, are also sceptical of the pieties of the European project. Both are fans of Lady Thatcher and tend to see the EU as the producer of pointless regulation and ill-conceived political schemes.

Going against a strong old grain

It is notable that some senior Italian politicians are thinking this way. But it probably does not reflect a real change in the country at large. Most of Italy's ruling class remains solidly “pro-European”. This month the Senate voted 212-2 to endorse the proposed EU constitution just produced by a convention in Brussels. Italian public opinion, unlike Mr Berlusconi, was strongly against America's war in Iraq. And pan-European opinion surveys still consistently show that Italians have more faith in European institutions—and more desire for political integration—than most other Europeans.

If top European politicians continue to treat Italy's prime minister like a skunk, more Italians may turn against the EU, particularly since Mr Berlusconi's media like to portray insults aimed at the boss as slurs on the Italian nation as a whole. But it is equally possible that Mr Berlusconi himself may be seriously damaged by his rows with the Union. Many of the criticisms of the prime minister that are never fully aired in Italy—or are dismissed as part of a left-wing plot—take on an extra force when relayed by the European press. Isolating your country within the EU is politically dangerous too. It helped destroy Mrs Thatcher (as she then was), even in a country as naturally Eurosceptic as Britain. It would be even more hazardous for Mr Berlusconi, in a country as historically warm to the EU as Italy.

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Intelligence and Iraq

The war isn't over for Tony

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But the prime minister's defensive strategy has shifted

IT WAS never realistic to hope that the report of the Commons foreign affairs select committee would settle the row over the government's use of intelligence material in the months leading up to war with Iraq. And, as expected, it didn't.

Alastair Campbell, the head of government communications, was cleared of the BBC's allegation that he had “sexed up” the first, substantial, dossier on Iraq's weapons of mass destruction. But only sort of. Unfortunately for Mr Campbell, the committee divided on party lines, five of its members saying they didn't have enough information to resolve the issue.

The rest of the report was similarly inconclusive. There was some criticism of the prominence given to the claim that Iraqi WMD could be readied within 45 minutes. The second dossier (or “briefing note”, as the government now calls it) that had been partially plagiarised from an academic thesis was “almost wholly counter-productive”. The prime minister, the committee concluded, had sincerely believed that there had been a “real and present danger”, but he had, unwittingly, misled Parliament over the provenance of the so-called “dodgy dossier”.

To be fair, the committee, as it recognised, had neither the time, the resources, nor the access to delve deeper. It came closest to the heart of the matter with its innocent-sounding suggestion that the government might like to say whether, in the light of events, it still believed the contents of the first dossier to be accurate.

It got its answer later in the week when the Commons liaison committee, a kind of super-committee on which every select committee chairman sits, had the chance to interrogate the prime minister directly. If anyone had been expecting to find Tony Blair rueful or apologetic, they were quickly disabused.

Asked whether he agreed with the foreign affairs committee's rather mild comment that the “jury is still out” on whether the threat assessment had been accurate, Mr Blair replied, “for me, the jury is not out.” He stood by the case presented by the intelligence services “totally”, while also “totally” refuting any suggestion that he had “misled either Parliament or the people”. He was quite sure that “we did the right thing in removing Saddam Hussein” and maintained that he had “absolutely no doubt at all that we will find evidence of weapons of mass destruction programmes”.

But for all his bluster, Mr Blair did change tack in one important respect. He is now talking about finding “programmes” rather than the weapons themselves. In this, he is quite likely to be proved right. But it is a rather different claim to the blood-curdling picture painted in the first dossier. Programmes might turn out to be little more than some teams of scientists who had the knowledge and ability to start re-building Iraq's arsenal if ordered to do so. If this is what the threat turns out to have been, the intelligence services will look foolish and Mr Blair reckless in not having exercised greater caution.

The growing possibility that there may have been such an intelligence failure is fuelling the calls from the Conservatives and Liberal Democrats for a judicial inquiry into the events and decisions that led to war. That would be so even if, like the Falklands war, Iraq was considered to have been a one-off—but it may not be. America has adopted as official doctrine the need to fight pre-emptive wars, while Britain appears to have a semi-official doctrine of always being there to lend a hand. This places enormous responsibility both on intelligence services to provide material that can be trusted and on their political masters to evaluate it soberly.

Mr Blair finds the idea of such an inquiry difficult, not because he feels remotely guilty, but because he cannot consider the possibility that mistakes may have been made, albeit in good faith and with relatively benign consequences. Refreshed after a relaxing summer holiday in the Barbados home of Cliff Richard, an elderly pop singer, Mr Blair would gain in stature were he to think again.

By comparison, the spat between the government and the BBC feels even more like the sideshow it always was. A few things, however, have become clearer in the course of the week. It now appears that the source for the “sexing up” story may have been a somewhat less central figure than was at first implied. Over-excitedly, the BBC thought it had something more sensational than it really was. It's an easy mistake to make. Ask Tony Blair.

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Iraq, Niger and uranium

Spies fall out

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Britain's spies are annoyed by an American retraction

THE relationship between Britain's and America's intelligence agencies is famously close. But British spies are not amused by the White House's public disavowal on July 7th of the president's claim in January that Iraq was seeking to buy uranium from Niger.

The problem for MI6 is a generous attribution in the state-of-the-union address. “The British government,” said President Bush, “has learned that Saddam Hussein recently sought significant quantities of uranium from Africa.” Now that, according to the International Atomic Energy Authority, some of the documents about Iraq's dealings with Niger have turned out to be forgeries, the White House's spokesman, Ari Fleischer, says, “knowing all that we know now, the reference to Iraq's attempt to acquire uranium from Africa should not have been included in the state-of-the-union speech.” The British, by implication, dropped them in it.

British spies are furious. They had good information, they say, which was not forged—and what's more, they did not pass it on to Washington, because spook etiquette demands that the consent of any third party which provides information (probably another country's spies in this case) must be secured. At least they have their boss on their side. On July 8th, speaking to the heads of the House of Commons select committees, Tony Blair defended the reliability of the British intelligence on Iraq's quest for uranium from Niger.

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Manufacturing

The lessons of a closure

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The closure of a tractor factory says a lot about Britain

THE lawns are still being mowed, the 16-storey European headquarters will remain busy. But below it the Massey Ferguson plant is dying. The last tractor rolled out in December, and this month the last of 1,100 production jobs will go. Coventry will lose yet another part of its metalworking history, a relic of the legendary (and revolutionary and profitable) Ferguson tractor. Why—and what goes next?

AGCO, the American owner of MF, had had a rough time after it acquired the firm in the mid 1990s. Europe's tractor markets were dull, and not aided by Britain's mad-cow panic and then foot-and-mouth disease. In 2002, things improved. But, producing in four EU countries, MF still had idle capacity, especially at its Beauvais plant in France, making heavy tractors. Demand was soaring for the light tractors it built in Brazil. Coventry built a bit of both. Close it, shift the work to Beauvais and Brazil, and AGCO would gain $20m-25m a year. A year ago, it so decided, and told the unions.

Told, not consulted. When the unions complained of that, AGCO said it had acted perfectly legally. So it had: the British government has just announced plans to join the rest of the EU in requiring employers to consult their workers before such decisions. But that is not yet the British way, let alone the American one, laments an official of Amicus-AEEU, one of the two unions mainly involved.

Not that the unions were unaware of AGCO'S problems. Coventry had earlier been on short-time, and, as they had argued to AGCO, it needed new equipment. But why close now that the market was looking up? And why Coventry? AGCO pointed to the business logic, to the higher investment needed than at Beauvais, and to sterling's high level. The unions add Britain's mild labour law: British workers are not only easier to get rid of but cheaper. A strike ballot did at least win a rise in the pay-off terms, to £1,000—about three weeks' typical wages—per year of service.

That is the flip side of Britain's attraction for foreign investors; “easy come, easy go”, says a Transport and General Workers' Union official, sourly. Not so: once you've invested, no plant closure is easy. But read “less hard” and he has a point.

The real trouble, though, and not just MF's or Coventry's, is basic business logic. It is often more profitable to manufacture abroad. But not only for cost reasons, nor simply across the channel. The rising euro has cut relative costs in Britain. But it cannot undo past under-investment, as Kumar Bhattacharyya, of Warwick University's Warwick Manufacturing Group, points out, nor give British factories access to a big domestic market. Nor is today's euro zone the only competition.

Look at PSA Peugeot-Citröen, whose Ryton plant, just east of Coventry, has been a real success, recently working flat out to build over 200,000 cars a year, though it is now cutting output slightly as the market slows. But the firm's dreams are of the big new market it sees in the future EU countries of central Europe. It has just begun building a new plant in Slovakia, and, jointly with Toyota, plans another in the Czech republic: low-wage plants (a third of British levels, say) that could give Peugeot another 600,000 vehicles a year.

And one day replace Ryton? No, say the firm, its unions and Coventry's boosters alike. Peugeot has indeed been promised government aid for Ryton. But, to justify this to EU scrutiny, it has said that the Slovak plant could be expanded to a further 150,000 cars. Theory, maybe. But suppose its plans to raise global sales from today's 3.2m to 4m vehicles a year go sour? Sweating Ryton—and that's the word when you work four shifts, leaving little time for maintenance—would allow the plant, at a reasonable euro/sterling rate, to compete well with French ones. But how would either fare against central Europe?

The French plants might well be at the greater risk. But look wider, and long-term. American-owned Jabil Circuit, a former Marconi supplier, recently closed 400 Coventry jobs, transferring work to Scotland and Hungary. Can Coventry be 100% sure even of Jaguar, which builds its top-of-the-range cars there, but sells heavily abroad, and is owned by Ford? Maybe. The cars are very British, and customised, and the firm's headquarters and design centre are in Coventry, with close links to Professor Bhattacharyya's outfit. But a city that has already lost tens of thousands of manufacturing jobs, yet still has 23% of its workforce in that sector, could well worry.

Yet here comes a paradox. Is Coventry shivering? No. Its unemployment is only just above the national average. The business park that replaced the long-dead Standard car factory supplies more jobs than Standard did. A miracle? No, just the market at work, as new jobs replace old. But there is a catch. The men at Massey have been earning about £10 ($16.50) an hour. Incoming manufacturers pay about half that. The old assembly lines are dying, but there is a new proletariat.

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Squabbling Anglicans

Unholy orders

Jul 10th 2003
From The Economist print edition

The anti-gay lobby has got the Archbishop of Canterbury rattled

Reuters

Williams weeds out the pansies

THAT the affair of Jeffrey John should have ended badly for the man at its centre is not surprising. Since his appointment as suffragan bishop of Reading, Mr John has been barracked by conservative evangelicals who find his unrepentant homosexuality (however Platonically expressed) anathema. Rather more surprising, though, is the role Rowan Williams played in securing Mr John's resignation, and the way in which the Archbishop of Canterbury has since tried to justify his removal.

In a statement on July 6th, Mr Williams argued that the appointment of Mr John had imperilled the unity of the church. The threat was not just to the Church of England, he explained, but the whole Anglican communion, and in particular its branches in the developing world. He was presumably thinking of some comments by Peter Akinola, the leader of Nigeria's 17.5m Anglicans, who had said two weeks earlier: “I cannot think of how a man in his senses would be having a sexual relationship with another man. Even in the world of animals, dogs, cows, lions, we don't hear of such things.”

Why should the Archbishop of Canterbury pay any attention to such an outburst? For two reasons. First, the Nigerian Primate has powerful allies, both at home and abroad. Social conservatives in the Church of England, who are fast becoming expert organisers, had by June 25th set up a new network, Anglican Mainstream, to lobby against the appointment of gay clergy. Having obtained Mr John's scalp, they and other groups are turning their attention to Gene Robinson, an openly gay man recently elected bishop by the liberal Episcopalians of the United States.

The second reason why the Archbishop of Canterbury feels obliged to listen to his far-flung provinces has to do with the increasing centralisation of the Anglican communion. During the 1990s, Mr Williams's predecessor, George Carey, greatly strengthened links between national churches, in part by encouraging the Primates to meet more frequently and in part by raising the profile of his own office. He has bequeathed to the less evangelical Mr Williams an institution in which decisions taken in one diocese are subject to global scrutiny and comment, and in which the head of the church is expected to answer for the whole.

The domestic row over Jeffrey John was worsened by finance. As their leaders are keen to point out, evangelical parishes are the fastest growing in England, and the most proficient at extracting money from congregations. Christian Research, an independent group, reckons that the average evangelical church raised £84,000 ($135,000) last year, compared with £40,000 for the rest. As has become increasingly clear, some of them are prepared to threaten liberal bishops with the loss of dues if they don't toe the line on appointments.

Yet the real wealth of the Anglican communion lies not in zealous English parishes, but in polite American ones. Congregations in the United States stump up much of the cash for the decennial Lambeth Conference, where international disagreements are aired. They also send lots of money to the African churches that periodically threaten to break communion with them. In February, the enormously wealthy Trinity Church, in New York, gave $70,000 to improve the communications network of the Nigerian church. As Canon James Rosenthal, the Anglican Communion's spokesman, points out, it's a nice irony: the most liberal wing of the church giving a voice to the most illiberal.

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War stories

Blair's biscuits

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New insights into the war cabinet

EARLY reviews of Sir Peter Stothard's book “30 Days: a Month at the Heart of Blair's War”, have not been generous. Despite dogging Tony Blair's footsteps for a month this spring, critics argue, the former *Times* editor failed to find out much about goings-on at Downing Street during a crucial episode in the nation's history. This is to ignore some startling revelations about Mr Blair and his closest associates:

•In contrast to the besuited Bush administration, they are lousy dressers. On March 16th—a Sunday, admittedly—Sir Peter notes the appearance of the “bullish” John Reid, then party chairman, in builders' jeans and a black leather jacket. “As for the others,” he writes, “it was hard to keep the mind off their startling range of ‘smart casual’ and athletics kit.” Jonathan Powell, the prime minister's chief of staff, later turns up for work in a pink and green rugby shirt and trainers. It is a Monday, and John Prescott, the deputy prime minister, who has a theory about the sartorial tendencies of public school boys, seems somewhat peeved.

•They eat badly. The limitations of the prime minister's diet are explored in detail: as far as Sir Peter can see, he subsists almost entirely on fruit and Wagon Wheels. Only in the company of President Bush does he eat a nutritious meal, which may tell us something about the relationship between the two leaders (or not). The others are just as bad, regularly downing pizza, crisps and bacon sandwiches. “At the foot of the stairs there is a machine dispensing food too unhealthy for the team to eat—except at times of stress,” observes the author on March 17th. One dreads to think what might be in it.

•They talk about football interminably. Alastair Campbell, Mr Blair's chief spin doctor, manages two jokes linking Saddam Hussein to British football teams. He begins a third effort: “What's the difference between Jacques Chirac and Graeme Souness?” but is silenced by a flick of Mr Blair's hand, and we never find out the answer. This goes on until March 25th, when American troops get within 60 miles of Baghdad. Only then is the reader informed that “Iraq has temporarily replaced football as the favoured male metaphor.”

•Leo Blair, the prime minister's three-year-old son, has lots of toys—stuffed animals, toy trains, a plastic truck—some of which turn up in official meetings. He is a sweet little boy.

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Public services

Hooked on targets

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Ministers can't think of a fourth way

IN A speech on July 4th, Tony Blair admitted that the government too often came across as managerialist and technocratic. Nowhere has it displayed these characteristics more than in its obsession with targets to improve the public services. Speaking on the same day, Patricia Hewitt, the trade and industry secretary, accepted there had been too many targets and said that delivering better public services was not like delivering pizzas.

So is the government now easing up on targets? Not as far as those who have to meet them are concerned. Peter Neyroud, chief constable of Thames Valley Police, says “there is absolutely no rowing back from targets whatsoever”. Tony Wright, chairman of a committee of MPs that has been examining targets, says: “organisations on the ground are groaning under vast numbers of targets”.

The Labour government's original rationale for targets was to ensure that higher public expenditure led to better public services. The Treasury agreed to release extra cash only if spending departments signed up to demanding goals. The first group of targets was set in 1998; since then there have been two further rounds. Many overlap. Some run for years to come, some have been dropped. MPs scrapped this week over how many of the original batch have been met. But the real issue about targets is whether they are helping to improve the public services. So far there has been scant evidence. For example, resources have been poured into the target-laden health service but growth in hospital-based activity has slowed rather than quickened.

Doctors claim that targets have been counter-productive. In his final speech as chairman of the British Medical Association, Ian Bogle complained about “the suffocation of professional responsibility by target-setting” and criticised “a healthcare system driven not by the needs of individual patients but by spreadsheets and tick boxes”. Dr Bogle accused hospital managers of using “trickery and ruses” to please their political masters, citing the use of temporary staff during the week in March when a waiting-time target for A&E departments was being audited.

Making doctors cross may be no bad thing in the producer-dominated NHS. But Dr Bogle has a point. Targets are a crude managerial tool that can lead to perverse outcomes. Too many of them and they provide no clear guidance about priorities. Too few of them and the priorities they highlight overshadow other worthy goals. Too great a stress on them and meeting the targets becomes the overriding goal. Managers are then tempted to “game” the system, improving the figures but not the underlying performance.

Mr Neyroud says that he has to grapple with as many as 200 targets. Not only are there too many of them; some are quite unrealistic. He has chosen to set a 5% goal to cut domestic burglary this year in the Thames Valley region because the 11.5% reduction needed to meet the national policing plan is not feasible. He says: “There should be fewer targets and they should be more tightly focused on what can reasonably be delivered.”

Many of the flaws in the government's target regime stem from its drive to control from the centre. Colin Talbot, professor of public policy at Nottingham University, says: “If they are to be effective, targets must be agreed, not centrally imposed.” Nigel Edwards, policy director of the NHS Confederation, which represents NHS organisations, calls for “politicians to set the overall framework and national standards and to delegate detailed target setting to local level”.

The parliamentary committee Mr Wright chairs is expected to back the principle of targets but to advocate a drastic cull in their number. That would be better than just turning down the volume about

delivery and targets—the gist of ministers' new approach. Best of all would be genuine reforms to foster competition and choice in the public services, so that the consumer rather than the man in Whitehall drives improvement.

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Transport

Muddle of the roads

Jul 10th 2003
From The Economist print edition

Labour's transport U-turn

WHEN Labour came to power six years ago, it believed that it could wean motorists away from their cars. The deputy prime minister, John Prescott, pledged to reduce congestion by 6% by 2010 and increase rail passengers by 50%. “Judge me,” he challenged.

The verdict is not a kind one. Congestion is increasing sharply. The proportion of British roads subject to serious delay is three times higher than in Germany and five times higher than in France. As motoring costs are predicted to fall by more than 20% by the end of the decade, while bus and train fares are likely to increase by 20%, road congestion is bound to get worse.

There are only two possible responses: build more roads or restrain the growth in traffic. This week, Alistair Darling, the transport secretary, opted for the former, announcing the biggest road-building programme since Labour came to power—though in a cautious nod to the latter, he is launching a feasibility study “to look at the practicalities of road pricing for cars in future decades”.

The £7 billion building programme involves widening parts of the M1 and the M25 to eight lanes over the next decade. Money will also be spent on the M18, the M11, the M62 and the M42 (see map).

But hardly any transport experts think this strategy will solve Britain's congestion problem. The regional transport studies on which Mr Darling's new road-building plans are based, concluded that demand is so intense around London that charging must be introduced if the new road capacity is not to fill up with traffic at almost the same level of congestion.

David Begg, chairman of the government's Commission for Integrated Transport, called this week for the government to introduce a nationwide satellite system of charging with tolls ranging from 2p a mile on rural roads to 50p on the most congested urban roads. He warned that if by 2015 there were not a

pricing system in place, traffic would simply grind to a standstill on the most congested parts of the network. The sharp reduction in congestion in central London following the introduction of the congestion charge in February strengthens this case.

A report on transport published this week by Mr Begg's commission was understandably bleak. Mr Begg said the government had “overpromised and underdelivered”. Hardly surprising, then, that when ministers talk, as they so often do, of improving public services, they never mention transport.

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Interest rates

King's first cut

Jul 10th 2003
From The Economist print edition

Interest rates fall by a quarter point

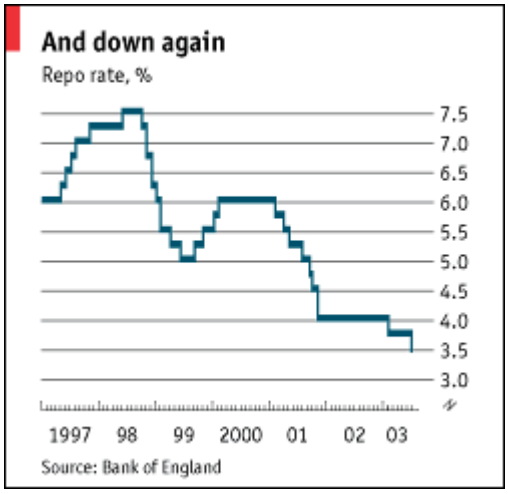
Get article background

MERVYN KING, the new governor of the Bank of England, has a reputation as a hawk. But within days of taking over from Sir Edward George, he has presided over a doveish cut in interest rates from 3.75% to 3.5%. This is the lowest rate for 48 years.

In a statement, the Bank said that the global economic recovery had remained “hesitant”: the outlook for exports was “weaker than previously expected”. Although inflation was currently above the 2.5% target, this was “the result of temporary factors which are expected to unwind in the coming months.” Pay growth had been muted so far this year.

The Bank also highlighted the fact that the exchange rate has recently regained ground after its sharp depreciation in the first few months of the year. This means there will be less inflationary pressure from the lower pound than it had previously feared.

Another factor influencing the monetary policy committee was that output growth in Britain has “recently been below trend”. Indeed the latest figures showed that economic growth at the start of the year was even slower than at first estimated. GDP grew by only 0.1% in the first three months of the year compared with the final quarter of 2002.



When a scandal affecting import figures was revealed earlier this week, some suspected it would affect the Bank's decision. An investigation by Customs & Excise has unveiled a fraud in mobile phones and computer components that has distorted figures for both imports and GDP. As a result, estimates for imports have been increased by £3 billion in 2000, £7 billion in 2001 and £11 billion in 2001. The effect on GDP has been to lower its level in the first quarter of 2003 by between 0.2% and 0.4% compared with earlier estimates. But the Office for National Statistics says that this will be offset by other revisions, leaving GDP broadly unchanged.

The Bank has not yet revealed the voting pattern. Mr King has voted against the majority in the past but will probably have voted for a cut this time.

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Aircraft noise

Dawn chorus

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Are night flights into Heathrow worth the disruption they cause?

Wakey wakey

AFTER four judicial reviews and two appeals to the European Court of Human Rights, the 20-year legal battle over night flights over London is no nearer a resolution. In a long-awaited judgment this week, the ECHR passed the buck back to the British courts to determine just how important a good night's sleep is.

So far, the courts have ruled in favour of the government only on the narrow issue that it had not acted unlawfully or irrationally in allowing night flights to operate into and out of Heathrow. On the wider economic issue, the government was forced to concede that it had made no attempt "to quantify the benefits of night flights or to draw up a balance sheet including the environmental disbenefits". Now the British courts will have to decide whether night flights are so important that they justify disturbing hundreds of thousands of people at dawn every day.

This issue sets a lot of cross Londoners on the one hand against big commercial interests on the other. No other major airport has a flight-path right across a capital city, and Heathrow is the world's busiest airport. But both BA, the airline which owns most of the crucial landing slots, and BAA, which operates Heathrow, say that the 16 night flights which come in between 4am and 6am are crucial. Most are from Asia and America, and are extremely profitable. Each scheduled night flight, according to the British Air Transport Association, is worth up to £30m a year.

Despite voters' anger, the government has always come down on the aviation industry's side. In 1993, the government replaced regulation based on numbers of flights with a regime based on noise which, critics claim, has led to a fourfold increase in night flights. A decade of failed judicial challenges followed, but official claims that noise levels were improving did not escape unscathed. Mr Justice Sedley, presiding over a judicial review in 1995, described one government consultation document as "a farrago of equivocation devious and deeply unattractive in its presentation and reasoning".

That pattern of behaviour appears to be continuing. The current night-flight regime, which has now been extended to 2005, is based on certified noise levels for different aircraft. But some planes, such as the Boeing 747-400, one of the most commonly used long-haul aircraft, are twice as noisy as their certified level, as research recently revealed by the Department of Transport has shown. Edward Lister, leader of Wandsworth Council, one of the boroughs under the flight path, claims that the government has known for almost four years that its figures were wrong.

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Bagehot

Tone alone

Jul 10th 2003
From The Economist print edition

The great consensus-builder finds himself alarmingly isolated

AFTER another bruising week, Tony Blair will be spending the weekend among friends. For at least a day or two, he will enjoy the balm of being surrounded by admirers and well-wishers. The occasion will be the Progressive Governance Conference, a spin-off from a think-tank chaired by Mr Blair's friend and former Northern Ireland secretary, Peter Mandelson, called the Policy Network. The conference, which Mr Blair's old chum, Bill Clinton, will kick off on July 11th at Guildhall in London, boasts the A-list of the international centre-left, including several past and present heads of governments. As testimony to Mr Blair's continued celebrity pulling power, it is an impressive line-up.

But the mood is likely to be darker than at previous gatherings intended to celebrate the politics of the "third way". For all the solidarity and mutual back-patting, the inescapable backdrop to the conference will be Mr Blair's mounting troubles. If this prime minister with his undeniable star quality, his unassailable parliamentary majority, his unambiguous mandate and sense of historic purpose is flailing, what hope is there for other centrist would-be modernisers?

What is most striking about the prime minister's predicament is how extraordinarily lonely it is. This week, making his twice-yearly appearance before the Liaison Committee, which brings together the chairmen of all the Commons select committees, Mr Blair was defiant and formidable. As Donald Anderson, the chairman of the foreign-affairs select committee, which this week issued its inconclusive report on the decisions leading up to the Iraq war, observed: "We tried to bowl him every kind of googly, but he just whacked each ball into the stands."

What the combined efforts of the Commons greybeards failed to do was penetrate Mr Blair's almost scary self-belief. Inevitably, most of the questioning was over Iraq. Sitting in Mr Blair's shoes, ordinary mortals might have felt just a little abashed at the failure to unearth a single weapon of mass destruction in Iraq after more than two months of searching. But the prime minister radiated the serenity that comes from the certainty that right is on your side. He had the air of Galileo addressing a college of cardinals, although in Mr Blair's case it was he, not his inquisitors, whose conviction seemed to be based more on faith than on evidence.

Even the most stalwart supporters of the war now part company with Mr Blair when he insists on the accuracy of the intelligence material that confirmed his belief in the threat posed by Saddam Hussein. Those who believe that the war was worth fighting mostly concede that it now appears that the threat was neither as great nor as imminent as was previously thought. Just as Mr Blair was virtually alone within the government in his determination to go to war alongside President Bush (even his closest advisers in Downing Street were a good deal more cautious than their master), he is now alone in his insistence on the validity of the narrow basis on which the war was fought.

This matters because unless Mr Blair is, at least to some degree, ultimately vindicated, the impression will grow that he is losing touch with reality. It was this affliction that, as much as anything, brought down Margaret Thatcher. Wanting something to be true does not make it so, even if you are prime minister.

Shaky foundations

Mr Blair's isolation over the war would be more bearable were it not mirrored in his domestic agenda. Hours after Mr Blair had put in his barn-storming performance in front of the Liaison Committee, the government, despite the frantic efforts of the Labour whips, beat off a rebel amendment to scupper

foundation hospitals, its flagship proposal for reforming the health service, by a mere 35 votes. With around 60 Labour MPs refusing to vote and 60 going into the lobbies with the opposition, this was the government's lowest majority since coming to power in 1997. Embarrassingly, had it not been for 40 Scottish MPs voting for legislation that does not apply north of the border, the government would have been defeated.

When the bill comes back from the Lords, where it is expected to undergo severe mutilation, it will be subject to further attack. What must be so dismaying for the prime minister is that even a relatively modest reform to give better-performing hospitals some limited freedom to manage their own affairs should be so fiercely resisted on ideological grounds by his own party. When Mr Blair tries to drive legislation through Parliament next year paving the way for differential university tuition fees, the ride is likely to be rougher still. While some Labour MPs can see virtue in foundation hospitals, very few indeed have been convinced by the government's arguments for making university students pay for their education.

Mr Blair will have his way with both top-up fees and foundation hospitals. If necessary, the whips will turn both issues into votes of confidence. But the idea that the prime minister is ready to accelerate the speed of public-service reform is a fantasy. The only people who believe it, apart from Mr Blair himself, are Stephen Byers and, of course, Mr Mandelson, but neither of those former cabinet ministers can these days do more than encourage from the sidelines.

When Mrs Thatcher wanted to extend privatisation through the economy and bury the trade unions, however controversial and divisive her policies may have been, she had no shortage of committed supporters to sustain her. Where are Mr Blair's? There are at most one or two in a cabinet that looks a good deal more Kinnockite than Blairite. In the lower ranks of government and sprinkled across the parliamentary party, there is, at best, a handful. The Labour Party has always been a vehicle for Mr Blair. But it is no longer one that is prepared to take him where he wants to go.

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Mergers

The return of the deal

Jul 10th 2003 | LONDON AND NEW YORK
From The Economist print edition

Do four billion-dollar bids in a week herald a new merger wave?

Get article background

PERHAPS British Airways is retiring Concorde too early after all. In its heyday in the 1980s and 1990s, the supersonic jet was full of investment bankers and advisers criss-crossing the Atlantic as they rode successive waves of mergers and takeovers. After the collapse of the merger market two years ago, Concorde was four-fifths empty (until the recent boom in “last chance” passengers). By the time it takes off for its final commercial flight in October, America and Europe could, on this week's evidence, be riding a merger wave worthy of the glory days of old.

Some $26 billion-worth of agreed and hostile bids have been announced since the start of this month. In the past week there have been four quite big ones. Alcan of Canada has bid *euro*3.4 billion ($3.9 billion) for a rival aluminium giant, Pechiney of France. EMC, an American data-storage company, has bid $1.3 billion for Legato Systems, an American rival. ArvinMeritor, a car-parts firm created by a merger in 2000, is bidding for the venerable Dana Corporation of Toledo. And Yellow, a haulage firm, is bidding nearly $1 billion for Roadway, a rival, continuing the global consolidation of logistics.

Several forces are pushing and pulling these takeover bids. On the push side are industries ripe for further consolidation, which has been delayed largely because of boardroom nerves and the horrid business conditions of the past three years. That has left lots of pent-up demand. The bid for Dana is a tidying-up exercise after a wave of smaller deals in the past decade that created ten global firms dominating the industry, supplying, as it happens, a similar number of big carmakers. Likewise the big aluminium bid is, in a sense, unfinished business from the three-way tie-up between Alcan, Alusuisse and Pechiney that was blocked by regulators in 1999 (see article).

The urge to merge

Similar mopping-up is expected in the travel and tourism business, as firms such as Le Meridien, a hotel group, and tour operators such as TUI, of Germany, and MyTravel, of Britain, seek salvation from the woes that have engulfed them since the September 11th terrorist attacks. Another European business

with an overhang of deals is the defence-aerospace industry. France's Thales could soon be in play when the French government seeks to sell its stake, and EADS (a Franco-German-Spanish aerospace group) seeks to round out its portfolio with a good defence-electronics business.

On the pull side, there is enough of a whiff of recovery in the air to stir animal spirits to do deals that have been pondered for a few years. Consider the technology industry, where leaders such as IBM, Cisco and Microsoft are awash with cash and hungry to make acquisitions that will take them into new markets by extending their technical reach. Similarly, Oracle's bid for PeopleSoft is likely to be only the first in a series of deals in an industry that is still splintered into hundreds of small and middleweight competitors, few of which seem likely to survive independently.

The financial markets have helped. Low interest rates and a more receptive corporate-bond market help companies that need borrowed funds to make acquisitions (see article). A sustained recovery in stockmarkets on both sides of the Atlantic has led firms to start paying for their purchases not just in cash, but with shares. If the stockmarket rally continues, rising share prices will lure in more buyers.

Some announcements have sparked bidding wars and other sorts of jostling, further suggesting that life is returning to the market. A couple of deals that had seemed to be done and dusted have suddenly become complicated again. In May, the owners of Selfridges, a once dowdy department store now revitalised as one of London's top retailers, accepted an offer of £598m ($980m) from Galen Weston, a Canadian retailer. But soon after the deadline for bids, Robert Tchenguiz, an Iranian property tycoon, entered the fray, before withdrawing again this week.

The sale of Hamleys, a large British toy store, also attracted a surprise rival bid. And some of the biggest media moguls have joined the auction of Vivendi Universal's American entertainment assets, even though the firm has decided not to include its Universal Music operation as part of the sale. Vivendi has picked five suitors to go through to the next round of bidding: NBC; Liberty Media (which has agreed to buy Comcast's majority stake in the QVC home-shopping network for $7.9 billion); Metro-Goldwyn-Mayer; Viacom; and an investment group led by Edgar Bronfman.

Vivendi seems certain to exceed the minimum price of $11.5 billion that it has set for its film, television and theme-park businesses. The struggling French conglomerate hopes to conclude a deal by September. But the auction could yet turn into an even bigger fight. A sixth potential suitor, an investment group led by Martin Davis, was dropped from the shortlist because its offer was considered unattractive. But that might not stop Mr Davis, an oil tycoon who once owned 20th Century Fox. He is rumoured to be considering a higher bid or concocting a deal with one of the five that have made the short-list.

Lastly, there is pent-up demand from the private-equity funds that, rather like company bosses, have spent the past couple of years sitting on the sidelines. In America alone, private-equity firms have over $100 billion-worth of equity to invest, a sum they can double or triple by adding on debt, says Steven Bernard of Baird, an investment bank that specialises in mid-market deals. Retailers are proving particularly tempting targets for private-equity investors. Many big stores occupy prime property locations, which have been increasing in value. These can be used to underpin the restructuring of balance sheets—in particular, by loading the firms up with today's cheap debt. Some or all of that debt can then be repaid by selling assets, such as property, that can be leased back for store use if necessary.

Will the boomlet last? The profits of many non-financial firms are still depressed, while capacity utilisation in America is at a 20-year-low—and even worse in the IT industry. Much of the recent run-up in share prices appears to be betting on a sharp recovery in corporate profits. If that fails to happen, share prices may slump and the pace of mergers slow.

Then there is the old, nagging question about whether mergers make business sense. Much navel-gazing followed the great merger frenzy of the 1990s, as boards of directors—their own mergers in ruins—solemnly dusted down old studies showing that mergers usually destroy value. Only this week, the Boston Consulting Group put out research showing that, of 277 big M&A deals in America between 1985 and 2000, 64% destroyed value for the acquirers' shareholders. (Interestingly, mergers in recessions or periods of low growth did better than mergers consummated in good times.) Still, that was 1985-2000. This, no doubt, is a new, more sensible, better managed era. It always is.

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Aluminium and antitrust

French twist?

Jul 10th 2003
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Will Alcan's bid for Pechiney get past the regulators?

IN THIS summer of corporate love, the unwanted embrace of Pechiney, a French aluminium company, by Alcan, its Canadian rival, could become a thorny romance. Alcan's offer recalls a friendly *ménage à trois* attempted in 1999 between Alcan, Pechiney and Alusuisse of Switzerland, which was rudely interrupted by offended European antitrust officials. Even so, Alcan went ahead with the purchase of Alusuisse.

Will this new, hostile attempt to complete the earlier threesome—thereby creating an aluminium giant to rival America's Alcoa—fare any better? Pechiney's board has rejected Alcan's offer as much too low, and is said to be seeking an alternative “white knight” buyer.

On its face, Alcan's pursuit of Pechiney makes sense. Along with the economy, the aluminium business has been in a slump; consolidation is in order. Alcan has yet to raise its bid, but is expected to do so. It has been playing to French pride, and to French unions' aversion to job cuts. Full-page ads in *Le Figaro* argue for the deal by highlighting Alcan's long history in France and the Québecois firm's “francophone culture”.

So how will the EU's antitrust watchdogs respond this time? In the years since Alcan's 1999 bid, the team headed by Mario Monti, the competition commissioner, has been buffeted by a series of successful legal challenges to its merger-blocking decisions. In one case, the European Court of First Instance declared baldly that the European Commission's merger analysis was “vitiated by a series of errors of assessment.”

Whether this will be enough to make it go easy on today's deals remains to be seen. Alec Burnside of Linklaters, a law firm, thinks that the commission is likely “to bounce back and show that the system still has teeth”. Already, it is looking hard at a bid by GE, which it once stopped from buying Honeywell, for Instrumentarium, a Finnish medical-equipment maker. The commission will certainly worry about the risk of collusion in a consolidated aluminium industry—a realistic fear in an industry already more integrated than for other metals, says Magnus Ericsson of Raw Materials Group, a consultancy.

On the other hand, Alcan has learned from its earlier rebuff. It has come up with a plan to shed assets in Germany to pacify the commission. Moreover, its bid will be helped by the continuing pain in the industry, deriving in part from growing competition from aluminium suppliers in China and Russia. This new competition makes it harder to believe that a merged firm would wield excessive market power.

In the end, the decision may rest with Pechiney's shareholders and, above all, its executives. If they try to construct an elaborate defence on antitrust grounds, perhaps the bid can be blocked. But this would probably be victory at a price: Pechiney might prevent itself from making any future acquisitions of its own.

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Corporate finances

Less stretched, for now

Jul 10th 2003
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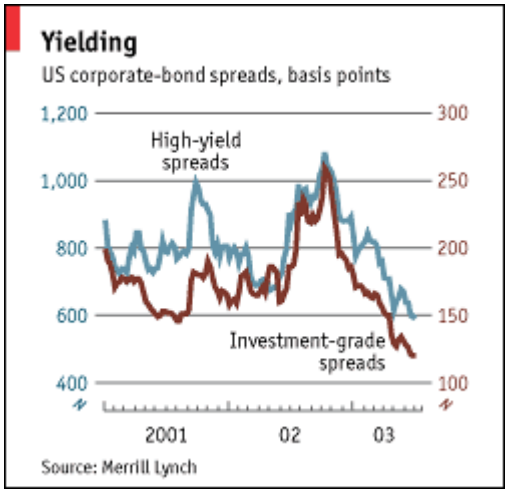
One reason why firms are now more confident is the bond-market "bubble"

THE date that still gives many a corporate treasurer nightmares is October 11th 2002. On that day, after months of scandal, bankruptcies and wrecked balance sheets, bond investors washed their hands of all but the safest corporate borrowers. The spreads on corporate bonds over Treasury bonds ballooned to historic highs, if firms could borrow at all. For many of the riskiest borrowers, credit markets simply shut down. An index of junk bonds compiled by Merrill Lynch rose to 1,100 basis points (11 percentage points) over Treasury bonds; even investment-grade bonds yielded 260 basis points more than government ones. Unable to afford such punitive rates of interest, many a firm seemed destined to go bust. As it was, by dollar value, more investment-grade bonds defaulted last year than at any time since the Depression.

As it turned out, though, this was the darkest hour. Investors' mood switched from fear to greed. Over the past few months, as risks have supposedly fallen, corporate-borrowing spreads have tightened faster than ever before (see chart). Firms have aggressively tapped the credit markets to make their financial position more secure—and, latterly, even to pay for acquisitions. Investors may yet come to rue their generosity.

Renewed confidence in corporate America has been reflected in a sharp decline in the number of new "fallen angels"—firms that have sunk from investment-grade to junk. This matters because asset-allocation rules prevent many big institutional investors from buying bonds that lack an investment-grade rating, and the rate of interest that firms must pay on new debt can rise alarmingly on mere worries that they might lose their investment-grade status. In the first half of 2001, some $89 billion of investment-grade debt was downgraded to junk, says Moody's, a rating agency. In the first half of 2002, this leapt to $107 billion. But in the first six months of this year, only $36 billion was downgraded to junk.



Investors have panicked several times in the past couple of years, fearing that some or all of the "big three" carmakers—together the biggest issuers in the corporate-bond market—would be downgraded to junk. Last October, spreads on their bonds (Ford's in particular) soared to levels that implied they were already junk. In the event, all three have clung on, but their actions suggest they do not think it will be for long. In late June, General Motors crystallised its huge pension liability by putting it on the balance sheet and issuing a record $17.6 billion of bonds to cover it. "It would not have been able to do that in the risk environment of six months ago," says Louise Purtle, an analyst at CreditSights, a research firm. And, she argues, GM did it now because it might not have been able to do it later. Speculation is rife that Ford will follow suit.

Some of the most dramatic recovery stories concern those firms that had already been downgraded. Many utilities were virtually shut out of the credit market after Enron's demise. Reliant Resources, which is now rated junk of an especially lowly sort, was one. But a couple of weeks ago it managed to raise over $1 billion in bonds at a mere 600 basis points over Treasury bonds. Mirant, an even more troubled energy firm, is completely restructuring its finances, and swapping debt for equity.

In technology and telecoms, too, there has been progress. Nextel, a telecoms firm, issued a $175m convertible bond in early June (which will look like cheap debt if its shares fall, and cheapish equity if they rise). DoubleClick, an internet advertising company, has raised $135m in convertible bonds. EDS, a

computer-services firm which by some quirk of fate still carries an investment-grade rating, recently issued $600m of convertibles and $1.1 billion of straight debt at just under 300 basis points over Treasury bonds.

Why have lenders become more confident? The Federal Reserve's readiness to cut short-term interest rates has helped. So have the efforts of chastened companies to do something about their stretched balance sheets. Troubled telecoms and technology firms, along with utilities, have busily sold assets to pay off debt.

European corporate debt has also been snapped up in recent months—notable beneficiaries include France Telecom, which was able to avoid becoming a fallen angel. Nor has the easing of credit markets stopped firms such as Vivendi, a troubled French conglomerate, seeking to offload assets to cut debt. Some of Europe's large, debt-laden telecoms firms can borrow more cheaply than they otherwise might because lenders assume they are backed by the state. This week KFW, a German state-owned bank, issued bonds that might allow it to sell a big chunk of Deutsche Telekom, thus reducing state support.

But European firms still rely far more heavily on banks than do their American counterparts. And in America, all the recent activity in the corporate-bond market has not reduced the overall leverage of companies. On the contrary. Moody's KMV, a research firm, has cranked the numbers for the 224 firms in the S&P 500 that issue significant amounts of bonds. Since last autumn, debt has risen from 35% of their balance sheets to 40%. “Firms are spending more than they are generating,” says Mac McQuown, the “M” in the firm's name. Yet KMV's estimates of default risk have fallen, because firms' assets are less volatile, or, put another way, there is less uncertainty about their businesses. This makes bondholders more confident that they will get back their money.

The entire atmosphere surrounding corporate America has become less febrile. This year there has been no Enron or WorldCom, and only a few examples of lesser book-fiddling. One much-watched guide to this new calm is the Chicago Board Options Exchange's Volatility Index, called VIX. This has dropped from over 40% late last year to just over 20%. Uncertainty, on this measure, is down by half.

Whether it will stay low is another matter—though who can tell what sort of shock it would now take to unsettle investors? If the pick-up in merger activity continues, credit quality may deteriorate. Interest rates might rise. Long-term rates are already up by half a point from their lows in mid-June. How many companies have managed to take advantage of the present enthusiasm for debt to increase the maturity of their liabilities, reducing their sensitivity to rising rates? Many utilities and telecoms firms have yet to do so, alas, and will instead have to refinance in the next two years, possibly on crippling terms.

Many of the firms with debt that investors have been so keen to snap up are exactly the same ones whose prospects they were so afraid of just a few short months ago. Many are in industries plagued by overcapacity and deflation risk, which is terrible for profits. Telecoms and airlines are well-known for their deflation troubles, but the same may hold for carmakers. Overcapacity in America's car industry exceeds 20% and is growing; sticker prices have been falling by a real 1% a year since the mid-1990s. One now seemingly forgotten lesson of that decade is to beware of companies that most need the money.

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Expensing share options

Out of options

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From The Economist print edition

Microsoft kicks a terrible habit

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AP

Happiness is their only option

OF ALL the good ideas put to bad uses in corporate America, share options are among the very worst. Although in theory compensation tied to a future increase in corporate share value is a sound idea, an award of options is the sole form of compensation that under American accounting standards does not have to be deducted from profits. Thus for many firms it became a way to hide an expense so that, superficially at least, it appeared to come without cost. For over a decade a huge battle has raged around reversing this state of affairs, primarily pitting technology firms against regulators.

On July 8th, Microsoft, the biggest tech firm of all, announced that it would forgo share options in the future—a staggering announcement by a firm almost as famous for making millionaires out of its employees (in large part due to share options) as for writing software. Given Microsoft's position in the tech industry and American business, its decision should prompt discussions at every company's board meeting. It seems highly likely that some other big firms will soon follow Microsoft's lead.

There are legitimate questions about how to value options awarded by firms to employees, and that uncertainty has been seized upon by those opposed to any number being attached to their cost. Rick White, chief executive of TechNet, a Silicon Valley lobbying group with 200 members, including Microsoft, says the tech industry remains strongly in favour of options—for their motivational powers—and of the current accounting (non-)treatment. Cisco and Intel are unlikely to follow Microsoft. The Financial Accounting Standards Board reckons the treatment of options should change because quirks of disclosure should not drive business decisions. Options are a form of compensation and should be treated as such, says Robert Herz, its chairman—yet no change will come before next year, if then. Congress, which in 1994 stopped FASB requiring proper accounting for options, is probably against it still.

Like any insidious addiction, once one firm in an industry granted options it became difficult, if not impossible, for others not to follow suit. No company, after all, wants to report lower profits than a competitor, particularly if the disparity can be erased with a stroke of a pen. And yet, if there was ever a painless moment to end an addiction, it is now. Microsoft's chief executive, Steve Ballmer, said he took the decision not because of the usual problems associated with providing options, but rather to remove the “angst” of employees about their compensation.

In late 1999, when Microsoft's shares were at their peak, any effort to eliminate options would have produced a mutiny. Not any more. As many as half of the options granted in the past by Microsoft do nothing more than allow employees to buy shares at a price above where Microsoft now trades (though they retain some value because the share price may yet rise above the strike price again). Recently, Microsoft's top executives have been dumping their own firm's shares, a reasonable way to mitigate risk, but also a sign that they are far less willing to tie their future prosperity to gains in share price.

Meanwhile, investors have begun to understand how badly options can distort reality. Merrill Lynch estimated that last year an average company's reported profits would have declined by 10% if options had been put in the accounts, and the average technology company's profits would have fallen by 60%. Microsoft acknowledged that its own profits would have been cut by a third had its options been similarly

treated. This may partly explain why Microsoft's p/e ratio of share price to profits has fallen from 86 to 30.

In place of options, the firm says it will now grant “restricted stock”—shares that will be fully transferred over five years. Their cost will be reflected directly on the income statement. While profits could suffer, the fact that the financial implications of the awards will be clear should ensure they are awarded with care. Investors, including employees, should applaud.

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Mobile telecoms

Doing the walkie-talkie

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Are “push-to-talk” calls the next big thing in wireless?

Get article background

FEW people have anything good to say about America's fragmented mobile-telecoms industry. Coverage is, by European standards, atrocious, despite boasts from operators about the quality and reach of their networks. Customers have to contend with complicated roaming arrangements, baffling billing terms, and bulky handsets. Text-messaging is still a rarity. But in one area, America leads the world.

In 1996 the country's fifth-largest carrier, Nextel, launched an obscure network technology, called iDEN, made by Motorola. It has a unique feature: a “walkie-talkie” mode that allows Nextel subscribers to talk to each other instantly merely by holding down a special button and speaking into the phone.

For years, this “push-to-talk” (PTT) feature, used mostly by builders, maintenance technicians and safety workers, was seen as an anomaly. Nextel was derided for going down a technological dead end with its choice of network technology, which is outside the two main global standards, GSM and CDMA. But now the tables have turned. As it searches for new services to attract customers and boost revenues, the mobile-telecoms industry has decided that PTT is the next big thing.

Subscribers like PTT because they can get through to somebody straight away. Operators like it because they can charge a premium for it. Other American mobile-phone companies envy Nextel's average revenue per user, an important industry metric, of $67 per month, way above the average of $54. Subscribers are also less likely to defect to other operators once they have become dependent on PTT. Nextel's churn rate is 1.9%, compared with a national average of 2.4%. No wonder rival American operators are now racing to add PTT to their existing networks.

First to launch a rival service is expected to be Verizon Wireless, America's leading wireless operator. Its PTT service is now being tested, and could go live this month. AT&T Wireless is expected to start testing soon, with other American operators to follow. Rising to the challenge, Nextel is upgrading its service to provide nationwide (rather than just regional) PTT calling, backed by an aggressive advertising campaign. It has also trademarked the terms “push-to-talk” and “PTT” and says it will go to court to stop other operators using them. Verizon, meanwhile, has launched a lawsuit against Nextel, accusing it of unlawfully obtaining a prototype Verizon PTT handset and engaging in “corporate espionage” by making test calls.

In the short run, at least, Nextel has little to worry about. Adding PTT to an existing GSM or CDMA network is fiddly. Most subscribers will require new handsets, and operators must ensure they have sufficient data capacity on their networks since PTT calls are handled as packets of data, not as traditional voice calls. And compared with Nextel's service, which connects users almost instantly, it can take two seconds to establish a PTT connection over a GSM network, and four to six seconds over CDMA, says Bob Plaschke of Sonim, a firm selling PTT upgrades to operators.

But although operators' original motive for adopting PTT was just a desire to imitate Nextel, says Phil Marshall of Yankee Group, a consultancy, it is now seen as a service that will appeal to teenagers and expand the market. “Nextel's solution is wonderful for plumbers who say ‘Harry, bring me the pipe' a hundred times a day, but that's 10% of the market,” says Mr Plaschke. He claims his firm's PTT system, which works on GSM and CDMA, has several advantages over Nextel's, including the ability to see if somebody is available before trying to talk to them. To appeal to teenagers, PTT will probably be marketed as “voice instant-messaging”, or “voice texting”, says Jason Chapman, an analyst at Gartner, a research firm.

Will PTT end up being used in America in the way that text-messaging is elsewhere, further widening the gulf between America and the rest of the world in wireless use? PTT advocates insist that it will take off in text-loving Europe and Asia as well, because there are times (such as while driving or walking) when texting is impractical. Several European operators are already looking at PTT. Nokia, the world's leading handset maker, says interest in the technology is widespread. Then again, it could all just be more hype from the mobile industry, which is always looking for something new to revive its fortunes. It may be able to talk the talk, but can PTT walk the walk?

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Beer innovation

The Eagle has landed

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Uganda's popular new local brew relies on a heretical brewing innovation

IN UGANDA, a cold lager after work is an expensive luxury. Until recently, the main alternative was a cloudy, foul-smelling and sour brew made by local families. But now an innovative new local lager is challenging these rivals—leading some to wonder if it will change the way that beer is made everywhere.

Since last December, Uganda's Nile Breweries, which is owned by SABMiller, the world's second-largest brewer, has been selling a new kind of clear lager called Eagle. This has been “wildly successful”, says Mitch Ramsey of SABMiller. It has already become Uganda's second-favourite beer, with a 30% market share, and it is still not available in Kampala, the capital, because the brewery cannot produce enough of it yet.

Its appeal, explains Mr Ramsey, is that it is an aspirational product, which both looks and tastes like a rich man's beer, yet is closer in price to the traditional local brews. There are two main reasons for its affordable high quality. It is made of locally grown grain called sorghum, instead of imported barley (barley does not grow well in much of Africa), which is particularly expensive due to a weak Ugandan shilling and high excise duties. But the real breakthrough is a pioneering method of brewing that avoids the long and costly malting process.

Malting, or sprouting and drying the seed, is the traditional way of turning the starches found in grains such as barley into the sugars that are then converted into alcohol. But, in a practice that many beer drinkers may see as treason, Nile Breweries converts the starches in sorghum by adding cheap industrial enzymes to the mash. Enzymes, proteins which catalyse specific reactions, are already used to convert, say, corn starch into corn syrup. Using enzymes to convert starch to sugar in Eagle beer gives the brewery a cost saving of 10%. With cheaper local ingredients, Eagle can sell for two-thirds the price of other local lagers, around 1,200 Ugandan shillings (roughly 60 American cents).

There is surely potential for this technology to catch on elsewhere in Africa. Even brewers in rich countries may one day be tempted to abandon malting for a 10% saving on manufacturing.

But how does it taste? *The Economist* assembled some highly trained in-house lager experts at its offices in London and put Eagle in a blind tasting against another beer (Stella Artois, a premium lager brewed in Britain). Most tasters correctly identified the “Euro lager”. Eagle was judged to be “intriguing”, “distinctive”, “alien” and more “bitter”. Several drinkers remarked that there was an unpleasant chemical bouquet. But their trained euro-palates may not be good judges. The extra bitterness is deliberate—it is something market research found a taste for in Uganda. Certainly, Ugandans have no trouble getting it down.

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The Volkswagen Beetle

The last love bug

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Finally, it is the end of the (production) line for the Beetle

SOONER or later, it had to come: 21m cars on, the absolute, definitive, final curtain for the Volkswagen Beetle. The Mexico factory of the German car firm has announced that it is to produce the last love-bug later this month. A final, limited edition (retro paint, white tyres and all) comes out on July 10th.

This news may come as a surprise to the rest of the world which, after all, moved on from its fond embrace of the bone-shaking, ear-splitting “people's car” many decades ago. The last Beetle was produced in Europe in 1978. But in Mexico, the holy union between Beetle and people has never been broken. So popular was the *vocho* (as it is known locally) that at one time, says Volkswagen, it accounted for over a third of all cars sold in Mexico. Even today, there are still 80,000 *vocho* taxis on the streets of Mexico City. Add to that 90 or so *vocho* “collectors' clubs” and a magazine, *Vochomania*, for bug-lovers.

Cynics suggest that the popularity of the car was a testimony more to the dreadful state of Mexico's roads than to the enduring excellence and smooth gear-changing of the vehicle. Whereas in the rich world the Beetle achieved a more fleeting popularity as the transport of choice for the counter-culture, in a country such as Mexico it was the car's qualities of robustness and reliability that ensured its continuing appeal.

But even the Beetle has now succumbed to market forces. In recent years, production at the giant Volkswagen plant in Puebla, just outside Mexico City, has dwindled to a mere 53 a day. Since 1994 and the start of the North American Free-Trade Agreement, Mexican consumers have been taking full advantage of the greater choice in the car market. General Motors and Ford have been offering cars, for about the same price as a *vocho*, into which one can actually climb and have a civilised conversation over the sound of the engine. Their models also provide air-conditioning without having to take out the windows, and air-cooled engines without removing the back of the car. Even Volkswagen seems slightly perplexed by the longevity of its car, scarcely altered since the first production model of 1937.

As well as the Jetta model, the Puebla plant now produces the “New Beetle”. But only 5,000 of these were sold in Mexico last year. Despite the name, Volkswagen says that this car is aimed at a different market from the *vocho*, and most are exported to Europe. The race is open to rear a new generation of Mexicans on a new car. And for the wrinklies who cannot bear to be parted from their bug, the good news is that Volkswagen has pledged to keep producing spare parts for the next ten years.

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Face value

In praise of trial lawyers

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How Bill Lerach, a hated American lawyer, became a corporate-governance hero

IS BILL LERACH on the side of the angels? The mere idea may turn most American businessmen an apoplectic purple. This, after all, is the man who, with his partners at Milberg Weiss Bershad Hynes & Lerach, has built a career on championing the shareholder lawsuit, a legal device that most American bosses see as a form of legalised extortion. But not everybody in America loves to hate this cuddly-looking trial lawyer. (Beware of appearances: his nickname is “king of pain”.) Mr Lerach and his partners have spent the past couple of years making friends in surprisingly influential quarters. Such has been their success that the firm may have become too big to manage, and could soon split. Mr Lerach's stature, however, continues to grow. Some of his supporters have even begun to champion him as America's best hope for corporate reform.

Ironically, Mr Lerach owes much of his new standing to a law designed partly to kill him off: the Private Securities Litigation Reform Act of 1995. This introduced several measures meant to make it harder for trial lawyers to encourage shareholders to sue companies, their directors and their officers for fraud. They included a requirement that control of a lawsuit go not to the client of the lawyer who files the case first, but to the shareholder with the biggest loss. Meant to stop lawyers from dreaming up cases, then trawling the streets for likely plaintiffs, its effect was to force Mr Lerach to seek out clients among institutional investors.

At first, the institutions ignored him. But once the stockmarket bubble had burst, they found Mr Lerach's theories of fraud—meticulously detailed schemes of personal enrichment that had the boss talking up the share price, cashing in his stock options, then letting the whole artifice collapse with a profit warning or a big write-off—suddenly, and shockingly, credible.

Mr Lerach has two main messages for America's institutions. First, the 1995 act, with other attempts to curb shareholder suits, fed the surge in business fraud during the bubble. Unencumbered by the threat of lawsuits, bosses had more freedom than ever to indulge their greedy, fraudulent impulses, he argued. Second, with the backing of the institutions, Mr Lerach believes he can improve the system, by forcing companies to reform themselves as part of the settlements that his law firm negotiates.

As one dimension of this effort, Mr Lerach has retained the services of Bob Monks, perhaps America's most distinguished corporate-governance activist. Earlier this year, Mr Lerach and Mr Monks settled a suit against Sprint, a troubled telecoms company, that included striking changes to the firm's corporate-governance practices, plus the departure of Sprint's top two executives. But the real test will be Mr Lerach's suit against Enron and its advisers, as this has a far more ambitious goal: the way in which Wall Street underwrites securities.

Hot on the heels of the $1.4 billion “Wall Street global settlement”, and another $1 billion settlement of lawsuits over initial public offerings, Mr Lerach's targets are the biggest names in investment banking: Citigroup, J.P. Morgan Chase, Bank of America, Goldman Sachs, Merrill Lynch, et al. Mr Lerach's lead plaintiff against Enron is the University of California, a conservative, highly respected institutional investor with no prior record of grandstanding or politicising governance issues. First and foremost, says the university, it wants its money back. Mr Lerach's opening proposal to the banks—thought to be a staggering $15 billion—would certainly achieve that. But Mr Lerach also says that his fees (typically 12-

15% of an award, but less on Enron) are based, in part, on whether he can force the banks to stop indemnifying themselves against their due-diligence failures as underwriters of securities. These indemnification agreements throw liability for due-diligence failures back on to the company issuing the shares or bonds, making a nonsense of an underwriter's gatekeeping role. The more banks Mr Lerach can persuade to drop these agreements, the more money he will make.

This is overtly self-serving. Mr Lerach's introduction of corporate-governance reforms into settlements helps him win round conservative judges (who, because settlements usually transfer funds from a company, already owned by its shareholders, to the same shareholders, minus fat legal fees, have tended to see shareholder suits as a negative-sum game). Strikingly, apart from Mr Monks and the University of California, Mr Lerach's new institutional-investor friends tend to be backed either by labour unions or by the public sector. Both are natural political allies: Mr Lerach is said to give generously to the campaign funds of state treasurers, for instance.

In a class of his own

But who knows what really motivates Mr Lerach? His father, a stockbroker, was destroyed by the crash of 1929, and never recovered. “Bill is perfectly capable of carrying on a suit he thinks is right, even if it costs him money,” says Mr Monks.

Shareholders of bankrupt firms can only win by teaming up with Mr Lerach. Suits targeting bust companies and their advisers feature shareholder-plaintiffs who have already lost everything: economically, their legal action becomes a claim on the surviving estate, which would otherwise be divided up among creditors. Suits against non-bankrupt companies, on the other hand, really do engineer a transfer of shareholder funds from one pocket to the other. For them to make sense for shareholders, the corporate-governance pay-off must be tangible.

The jury is out on Sprint. Even Mr Monks concedes that “we got lucky”—the board had already decided to jettison the top two officers. Those indemnity agreements, however, are a real prize—something that every sane institutional investor in the country would like to see ended. If that happens, the new alliance could go a lot further. As Mr Lerach says, “we can't let ourselves be victims of a lack of imagination.”

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Corporate strategy

Who gets eaten and who gets to eat

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Is recent history making companies timorous in their strategic planning?

WITH stockmarkets and profits both edging up, corporate executives are daring to think again about the future. Emerging from their cost-cutting bunkers and shaking off the excesses of the turn-of-the-century boom, they are talking once more about strategies for growth. Admittedly some companies—carmakers such as Ford and Fiat, for example, and many airlines—are still wondering how to survive. But others are already expanding. Japanese carmakers are opening new plants in North America. Some airlines, such as the low-cost carriers easyJet and AirTran, are buying large numbers of new aircraft. Emirates ordered no less than $12 billion-worth of giant Airbuses at last month's Paris air show.

Moreover, hostile takeovers are reappearing on the stage (see article), a sure sign of emerging opportunism. In software, Oracle is bidding for PeopleSoft; this week ArvinMeritor bid for a fellow car-parts maker, Dana, and Alcan went for Pechiney, a move that could trigger a consolidation of the aluminium industry.

As they search for growth opportunities, however, companies face a classic dilemma, one made more poignant by recent events: should they assume that the future will, more or less, be a continuation of the past; or should they try to anticipate the next big revolution? Should they, essentially, hang on to what they've got (their “core competence”), or should they strike out for a brave new world?

Hold the revolution

After the dotcom disaster and much idle talk of a new economic paradigm, revolutions are distinctly out of favour. Belief in rapid change and dramatic responses has been shaken by the bursting of the stockmarket bubble, and by the demise of such firms as Enron and Webvan. There is now a widespread aversion to management fads. Most managers today are more interested in getting the basics right than in chasing the next rainbow.

An article in the July issue of the *Harvard Business Review* reflects this spirit. Called “What Really Works”, it reports the findings of a five-year research programme (led by Nitin Nohria of the Harvard Business School and William Joyce of the Tuck School of Business). The study put 160 companies under the microscope over a ten-year period (1986-96), grading them on their use of some 200 different management practices. Its main finding is that superior performance does not depend on use of this or that trendy management technique. “It doesn't really matter if you implement ERP (enterprise resource

planning) software or a CRM (customer relationship management) system; it matters very much, though, that whatever technology you choose to implement you execute it flawlessly."

Flawless execution, claim the authors, is one of four old-fashioned things that distinguish successful companies over time. The other three are: a company culture based on aiming high; a structure that is flexible and responsive; and a strategy that is clear and focused.

One thing standing in the way of the flawless execution of clear strategies, writes Charles Roxburgh in the latest issue of *McKinsey Quarterly*, is the human brain. In "Hidden Flaws in Strategy" he applies some of the insights of behavioural economics to strategic decision-making. Management's tendency to be over-confident and to favour the status quo, he says, works against good strategic planning.

So too does the phenomenon of "anchoring", the linking of things people do not know to vaguely related things that they learnt recently. For example, ask somebody for the last three digits of their telephone number; and then ask which year Genghis Khan died. Most will give a three-digit date in the first millennium (when the answer is, in fact, 1227). "Anchoring can be dangerous," says Mr Roxburgh, "particularly when it is a question of becoming anchored to the past."

In their book "Creative Destruction", Richard Foster and Sarah Kaplan, two management consultants, make a similar argument. They say that too many corporate bosses assume the future will be much like the past—what worked before will work again—an attitude that can all too often destroy shareholder value. The authors tell the story of a Manhattan branch of the East River Savings Bank, founded in 1848, its Ionic columns exuding safety, security and thrift. But the bank went into the property market in the 1970s, was hit by the savings-and-loan crisis in the 1980s, and ended up in the hands of a property developer who sold the branch to another bank, which closed it in 1997. Today the building is a pharmacy.

Anchors aweigh

How then to weigh corporate anchors and move on from the recent past? Mr Foster and Ms Kaplan say that businesses should stop hankering after a mythical golden age, when enterprising firms grew gradually into solid companies in which widows and orphans could safely park their money. This rosy view of the corporate past is an illusion, they say. "The corporate equivalent of El Dorado, the golden company that continually performs better than the markets, has never existed. Managing for survival, even among the best and most revered corporations, does not guarantee strong, long-term performance for shareholders. In fact, just the opposite is true."

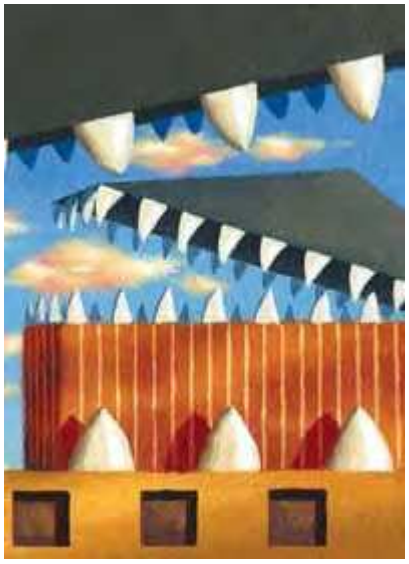
The two authors compared the original 1917 *Forbes* magazine list of the top 100 American companies (by assets, in those days), with a comparable list that the magazine published in 1987. By then, 61 of the original group had ceased to exist; of the remainder, only 18 had managed to stay in the top 100. They included such respected firms as Kodak, DuPont, General Electric, Ford, General Motors and Procter & Gamble. These all survived depression, world war, the oil-price shocks and unprecedented technological change.

But survival did not mean that they were more profitable than their peers. Of the 18, only General Electric and Kodak outperformed the stockmarket. The group as a whole had returns that were 20% below the market's compound annual growth rate of 7.5% over those 70 years.

A look at another list confirms the point. Of the companies that made up the S&P 500 in 1957, only 74 (37%) made it through to the 1997 list, and only 12 (6%) outperformed the index over the period. As Mr Foster and Ms Kaplan put it, by the end of the 1990s, an S&P 500 made up only of those companies that had been there since 1957 would have underperformed the actual index by one-fifth, year after year. Endurance *per se* bears little if any relationship to performance.

The subheading to Mr Foster's and Ms Kaplan's book is "From Built-to-Last to Built-to-Perform", a dig at one of the most influential business books of recent years, "Built to Last" by Jim Collins and Jerry Porras. Published in 1994, "Built to Last" looked at a small sample of companies (18) that had been persistently great over a long period of time. It suggested that endurance and performance were linked.

In his sequel, “Good to Great”, published in 2000, Mr Collins tried to pin down what it was that distinguished great companies from those that were merely good. His definition of a great company was one that had spectacularly outperformed the stockmarket by a factor of three over a 15-year period. This level was chosen because it was comfortably above the average 2.5 times by which acknowledged leaders such as 3M, Boeing, Coca-Cola, General Electric and Wal-Mart had outperformed the market from 1985 to 2000.



In a contrary way, Mr Collins and his team of researchers came up with a list of nine things that they had not found in their winning companies. Great companies, Mr Collins claims, do not depend on outstanding charismatic leaders, brilliant strategy or audacious takeovers to pull ahead. At the top they rely on quietly determined bosses with a belief in high standards and discipline.

One example is Darwin Smith, a chief executive of Kimberly-Clark, whose unassuming nature did not prevent him from taking dramatic decisions. At one stage he realised that the company's core business of making coated paper offered the prospect of no better than mediocre returns. So he sold the paper mills and bet the company on becoming a leading maker of consumer paper products.

A similar thing happened with another of the companies on Mr Collins's list of greats. Walgreens pottered along as a chain of 500 restaurants, based on the founding family's formula for malted milk-shakes, until the early 1970s. At that point, Charles Walgreen III decided that the company would do better if it were to focus entirely on drugstores. He wound down the restaurants within five years, and Walgreens went on to become a stockmarket star for the next 25.

This is a bit like Cortes burning his boats so that his men had no choice but to make their old-world ways succeed in the new world. There was literally no turning back. For Mr Collins, there is no conflict in remaining anchored to the past, but at the same time going for greatness in the future. He believes that leaders such as Mr Smith and Mr Walgreen did not start to make their companies great by setting a new vision and a new strategy. Instead, he says, “they first got the right people on the bus, the wrong people off the bus, and the right people in the right seats—and then figured out where to drive it.”

Inevitable surprises

Choosing the passengers before the journey is not a formula favoured by Peter Schwartz. The doyen of scenario planning—a widely used method for companies to think about the future, developed largely by the Shell oil company in the 1970s—argues that the future is not as unknown as we think. Companies can chart a route and then decide whom they need to steer them along it.

In his new book, “Inevitable Surprises”, Mr Schwartz lists some of the future shocks that should not surprise us—the lengthening of the human life-span, for example, where 60 becomes the equivalent of 40; the changing patterns of migration; the dominance of American economic and military might; and the existence of “a set of disorderly nations with the capacity to unleash terror, disease and disruption” on the rest of the world.

Companies that want to prepare themselves for these inevitable changes have a number of options, says Mr Schwartz. These include building effective intelligence systems; cultivating a sense of timing; and trying “to avoid denial”. They also include putting in place mechanisms to engender creative destruction. “What processes, practices, and organisations have you actually dismantled in the last year or two?” asks Mr Schwartz. “If the answer is none, perhaps it's time to get some practice in before urgency strikes.”

The idea that great companies stick closely to their past is also anathema to Fritz Kroeger, a vice-president at A.T. Kearney, a consulting firm, whose new book about strategy—“Winning the Merger Endgame” (written with two colleagues, Graeme Deans and Stefan Zeisel)—argues that the main factor determining corporate survival and success is the speed with which companies climb what he calls “the endgame curve”. This is basically a strategy of creative destruction via mergers and acquisitions. Or, as Sweeney Todd sang in the Stephen Sondheim musical, “the history of the world, my sweet, is who gets eaten and who gets to eat.”

An individual company's strategy in this game should, say the authors, be determined by the stage of life that its industry has reached, and there are, they claim, four distinct stages. In the first, there is little or no market concentration. Newly deregulated firms, start-ups and industries spun off from others are all present at this stage. Concentration, measured by the combined market share of the three biggest companies (CR3), is low—less than 20%. Industries currently at this stage, say the authors, include railways, telecoms, utilities and insurance, all of which Mr Kroeger thinks will stay in stage one for at least another five years.

The second, seven-year phase he calls the “scale stage”, when size begins to matter. Leading companies start to emerge, and concentration increases to around 30-45% on the CR3 scale. Industries that are now in this stage include chemicals, drugs, pulp and paper, fast foods, hotels and breweries.

In the third phase, Mr Kroeger says companies extend their core businesses, eliminating secondary operations or swapping them with other companies for assets closer to their core activity. By this point, industry leaders have come to account for nearly 70% of their market. Industries in this phase include steel, toys and tyre manufacturing.

Finally, there are a few companies that enjoy about 90% of their industry's worldwide market. The corporate titans of this fourth stage—in such industries as tobacco and automobiles—tend to form alliances in order to boost growth, which by now has become hard to find. Thus General Motors has 25% of the global car market, but only through its strategy of forming alliances with such other carmakers as Fiat, Fuji, Daewoo and Suzuki.

Challenging the status quo

Perhaps the biggest challenge for corporate planners today is, as Mr Roxburgh puts it, “to distinguish between a status quo option that is genuinely the right course and one that feels deceptively safe because of an innate bias”. That innate bias towards changelessness is stronger today than it was five years ago, before the stockmarket bubble burst and so many investment decisions were made to look foolish.

Mr Foster and Ms Kaplan call this innate bias “cultural lock-in”. It helps explain how John Akers, a dynamic computer-industry lifer by the time he became boss of IBM, could make such a mess of the job. All his energy, astuteness and intelligence (combined with those of his senior lieutenants) could not help him to see how his company was being swept into a waterfall by changes bubbling just beneath the surface of the industry.

On the other hand, there are those who have gone for creative destruction and ended up destroying themselves, and sometimes much else besides. Enron, for example, dispensed with its old business model of natural gas and pipelines to turn itself into a futuristic online energy trader. Of course, it is conceivable that Enron would have succeeded had it not, along the way, taken some lethal short-cuts.

Likewise, two traditional British companies, GEC and ICI, thought they could master radical change. Both shed solid old businesses and bet on acquisitions in higher-margin, growing sectors (telecoms for GEC, which renamed itself Marconi in the process, and specialty chemicals for ICI). But both came to grief because they borrowed too much and paid too much. For them, the status quo would have been much the better option.

At the end of the day, perhaps there is no better strategic advice on this issue than that of Giuseppe di Lampedusa's weary aristocrat in “The Leopard”. Struggling to survive the turmoil of 19th-century Italy, he wryly observed that, “everything must change, so that everything stays the same.”

Winners take almost all

One thing is for sure: whether companies stick with what they know or head into a maelstrom of creative destruction, the prizes for the winners are well worth having. Recent research by McKinsey shows that Pareto's Principle—the observation first made by a 19th-century Italian economist, Vilfredo Pareto, that 80% of national income ends up in the hands of 20% of the population producing it—is alive and well today. The so-called 80/20 principle applies to the value added by industrial companies as much as it does to the income produced by nations.

McKinsey examined a sample of 1,000 listed companies in America from 15 different industries over the period from 1969 to 1999, when companies experienced more wrenching changes in their environment than ever seen before in peacetime. They measured the market value added (MVA) by companies, the change in their outstanding debt and their stockmarket capitalisation. And they found that 80% or more of all 15 industries'MVA over the period was accounted for by the top 20% of companies. Moreover, this 80/20 split remained remarkably steady over the whole 30-year period, with only one significant blip—to 76%—in 1989.

The rewards for getting it right can be huge. But the punishment for getting it wrong can be death. A short walk through the West End of London today provides a salutary reminder of corporate mortality. On one side of the Thames at Westminster sits the deserted former head office of the once great British Steel, which is now melting down after merging with a Dutch firm. Across the river, a government regulator occupies what was formerly the proud headquarters of ICI, 30 years ago the epitome of British manufacturing, now a struggling rump. Near Hyde Park Corner, the former offices of GEC, another erstwhile icon, are now luxury flats. And on Bond Street, just up the road, the headquarters building of Marconi stands abandoned, the junk mail piling up behind its locked doors. All that's missing is the tumbleweed and a whistling wind.

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Asian currencies

Fear of floating

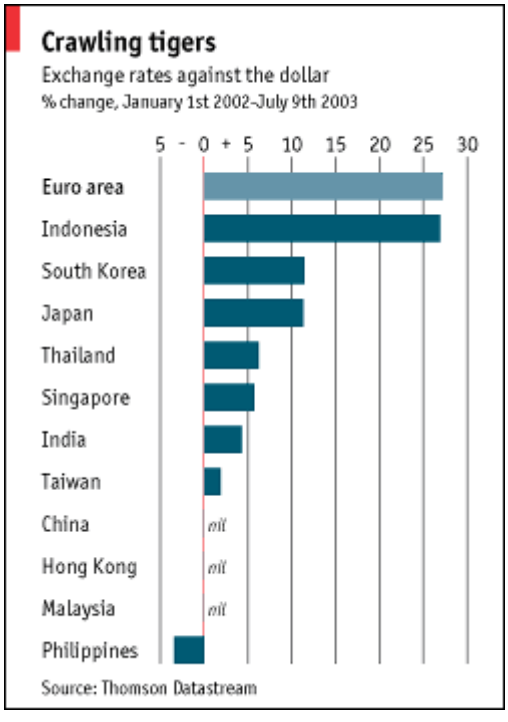
Jul 10th 2003
From The Economist print edition

AP

By tying their currencies to the dollar, Asian governments are creating global economic strains

AFTER sinking since the start of the year, the dollar has come up for air, gaining 4% against the euro in recent weeks. But it is quite likely to plunge again, pulled under by America's huge current-account deficit. So far the dollar's descent has been uneven. It has fallen by around a quarter against the euro since the start of 2002. But it has lost only 10% or less against the yen and many other Asian currencies, and it is unchanged against the Chinese yuan, although most of the Asian economies have large balance-of-payments surpluses.

America's biggest bilateral trade deficit is with China ($103 billion in 2002). Asia as a whole accounts for half of America's total deficit. If these currencies cling to the dollar, then others such as the euro will have to rise disproportionately if America's deficit is to be trimmed.

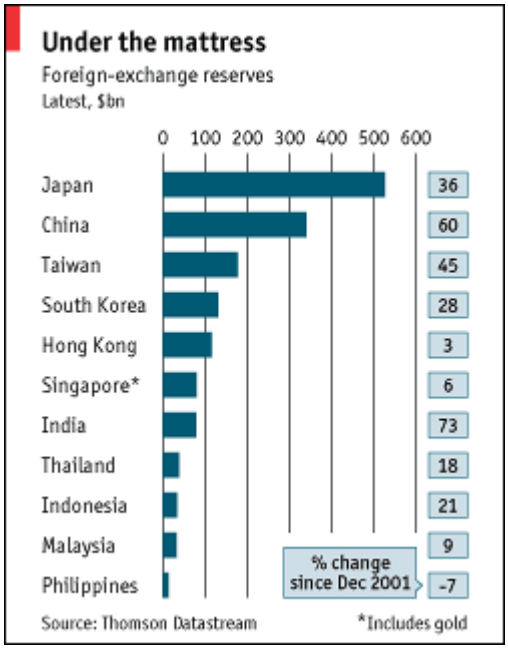


And cling they do. The Chinese yuan and the Malaysian ringgit are pegged to the dollar and protected by capital controls. The Hong Kong dollar is also tied to the greenback through a currency board. Officially, other Asian currencies float, but central banks have been intervening on a grand scale in the foreign-exchange market to hold down their currencies as the dollar has weakened. The exception is the Indonesian rupiah, which has gained 27% against the dollar in the past 18 months (see chart).

Whereas intervention to support a currency often fails, intervention to push one down can be more effective, because in theory a central bank can print unlimited amounts of its own currency with which to buy dollars. As a result of central banks' heavy buying, Asia's foreign-exchange reserves have swollen from less than $800 billion at the start of 1999 to over $1.5 trillion now, almost two-thirds of the global total. Japan bought over $30 billion-worth in May alone; it now has almost $550 billion in its coffers. The world's seven biggest holders of foreign-exchange reserves are all in Asia (see chart).

The Asian countries' reluctance to allow their currencies to rise against the dollar is coming in for increasing criticism. At a meeting in Bali last weekend of Asian and European finance

ministers, the Europeans urged the Asians to let their currencies rise. John Snow, America's treasury secretary, the International Monetary Fund and the Bank for International Settlements have all called for a stronger yuan.



Asian governments worry that appreciating currencies might hurt their exports. Yet many of their currencies are supercompetitive. As the dollar slides, their trade-weighted values against a basket of currencies is falling. According to *The Economist*'s Big Mac index, China has the most undervalued currency in the world. Using more sophisticated methods, UBS, a Swiss bank, reckons that the yuan is now more than 20% undervalued against the dollar.

UBS reckons that there are two tell-tale signs that a currency is undervalued. The first is rapidly rising official reserves. China, Japan, Taiwan and India have seen the biggest increases in reserves over the past 18 months. On the other hand, in Hong Kong, Singapore, Malaysia and the Philippines, reserves have been fairly flat.

A second test is the size of a country's basic balance (the sum of its current-account balance and net inflows of long-term capital, such as foreign direct investment). In 2002 China's current-account surplus was 2.2% of GDP; adding in foreign direct investment gave a basic balance of 6% of GDP. This year the current-account surplus has shrunk, but the overall basic balance remains well in surplus.

UBS reckons that all the Asian currencies, except Indonesia's, are undervalued against the dollar on the basis of these two measures. The most undervalued are the yuan, the yen, the Indian rupee and the Taiwan and Singapore dollars; the least undervalued are the ringgit, the Hong Kong dollar and the South Korean won.

In a free market, China's currency would surely rise. But demands from foreigners are likely to fall on deaf ears. The Chinese government is worried about rising unemployment as jobs are lost in unprofitable state companies, and deflation remains an issue. Moreover, until banks are reformed and non-performing loans tackled, it would be dangerous to liberalise the capital account. It would be safer to repeg the yuan at a higher rate. But most economists reckon that, at best, the yuan's band will be widened slightly over the next year, without allowing room for any significant appreciation. And, so long as the yuan is pegged to the dollar, other Asian countries will have a big reason to resist appreciation too.

In the wake of the Asian crisis of 1997, it is understandable that governments like to have bigger reserves to defend their currencies against future attack. But stuffing reserves under the mattress is not without cost. The return on American Treasury bonds is much less than could be had from investing the money more productively at home. Large inflows of foreign exchange can also bring too much liquidity into the economy, which can then cause asset-price bubbles. Asian central banks have tried to “sterilise” their intervention, selling bonds to mop up extra liquidity, but this will become harder as reserves grow.

China is considering various policies to stem the rise in reserves and fend off pressure for a revaluation. One option would be to allow firms to retain more foreign-exchange earnings; at present most have to be sold to the People's Bank of China. Another option is to relax restrictions on residents and firms wanting to buy foreign currency. The government already plans, later this year, to allow Chinese firms to buy foreign bonds. In June, 11 Asian countries set up a $1 billion Asian Bond Fund that will invest in local bonds. The aim is to develop local bond markets and so keep more Asian capital at home rather than see it invested abroad.

Fred Bergsten, of the Institute for International Economics in Washington, DC, criticises Asian countries' exchange-rate policies. He complains that they are not playing their role in the global adjustment process that is needed to reduce America's external deficit. As a result, as the dollar slides, the euro is likely to become seriously overvalued, while Asia's cheap currencies may provoke protectionism.

The complaints from Europe are likely to be louder than those from America. American pressure on China may be limited because the United States needs China's help in resolving tensions with North Korea. Another reason for America to pull its punches is that China and other Asian countries hold their reserves largely in American government securities. If Asians lost their appetite for dollar assets, the greenback

would fall even faster, and American bond yields would rise.

Indeed, from this point of view, the Asian economies are supporting America's profligate habits. By buying American government securities they help finance America's large external deficit, hold down interest rates, and so sustain the boom in consumer spending and mortgage borrowing. This may benefit America in the short term, but it allows even bigger imbalances, in the shape of consumer debt and foreign liabilities, to continue to build. The eventual consequences for America—and the world economy—could be more painful.

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About sponsorship

Government bonds

Letting off steam

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Some air comes out of government-bond markets

MOST people who care about such things were probably surprised when the yield on ten-year bonds issued by the Japanese government fell to less than 0.5%, the lowest in recorded history. Perhaps they were also surprised that ten-year American Treasury bonds should have yielded 3.1%—not in quite the same league, but lower than since Elvis was a tot.

Pundits detected a bubble, screaming that yields bore no relation to economic fundamentals. In fact, this is untrue: real yields are higher than in 1982, when ten-year Treasury bonds yielded 15.6%, because inflation has fallen. Still, the pundits seem to have been vindicated. In the past couple of weeks, government-bond prices have dropped sharply, driving up yields. Ten-year yields are now 3.7% in America, 4% in Germany (their highest in two months) and a juicy 1% in Japan.

Bubble or not, the behaviour of government-bond markets has been peculiar, especially in America. Until recently, the prices of bonds had been rising in tandem with stockmarkets (see chart). This has often happened before, because lower long-term interest rates make shares look cheaper. But this time the two markets appear to have been rising for diametrically opposed reasons.

Bond yields have been falling in part because of worries about deflation. Japan has lived with deflation since the mid-1990s, and the Bank of Japan has been unwilling or unable to do much about it. Now America faces the risk of deflation too. So, more markedly, does Germany. The thought that the price level might fall makes attractive any security that pays a fixed rate of interest and is redeemed at par, all the more so if central banks are likely to cut short-term rates.

In contrast, the threat of deflation ought to be bad for the stockmarket. It means that companies' revenues are unlikely to grow much. Deflation also raises the real value of debt, of which companies have plenty. Yet stockmarkets around the world have been having a fine time lately. Since its low in early March, the S&P 500 has risen by a quarter, and the tech-heavy NASDAQ has gone up by over 30%. In Japan, the Nikkei has risen to within a sniff of 10,000—admittedly, a mere quarter of its 1989 peak—for the first time since August last year.

Stockmarkets have been heartened in part by signs of growth, even in Japan. The group of soothsayers polled by *The Economist* expects America's GDP to rise by 2.3% this year and by 3.4% next. Most of this growth is forecast to manifest itself only in the second half of the year: J.P. Morgan, for example, now expects the American economy to grow at an annual rate of 4% in the third quarter and 3.5% in the fourth.

In a world in which investors are constantly switching between stocks and bonds, how on earth can the two markets go such separate ways? David Goldman, head of global markets at Banc of America Securities, likens it to Groucho Marx's horse doctor in “A Day at the Races”, who tells a socialite that she has “double blood pressure”: low blood pressure on the right side of her body and high pressure on the left. Unlikely, in other words.

So what explains the apparent divergence? One reason is that, worried about the deflationary threat, the Federal Reserve has, in effect, promised to keep short-term rates low for as long as it takes to see off

trouble. Because inflationary pressures are so muted, bonds benefit from this. But equities have gained too, because investors are betting that the Fed will be successful in the end.

Another reason for falling Treasury yields emphasises the role of Asian central banks, which have been buying dollars in an attempt to stop their own currencies going up. They have to put their money into dollar assets, and their assets of choice, for reasons of safety and liquidity, are treasury or government-agency bonds. Their purchases, goes the argument, have driven yields down.

Doubtless there is something, perhaps a lot, to be said for both arguments. But they still leave nagging questions. Foremost among them is: why are long-term interest rates still so low? If investors assume the Fed's ultimate success in its battle against deflation, such derisory yields seem odd. Japan had many a sharp stockmarket rally in the 1990s before its share prices reached new lows and its bond prices new highs.

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Bank Austria and Hypovereinsbank

Running repairs

Jul 10th 2003 | MUNICH AND VIENNA
From The Economist print edition

Short of money, a Bavarian bank sells part of its Austrian subsidiary

HYPOVEREINSBANK (HVB), Germany's second-biggest bank and Europe's biggest mortgage lender, is throwing out ballast to keep afloat. On July 8th it sold a quarter of its best-performing subsidiary, Bank Austria Creditanstalt, at *euro*29 ($33) a share, to raise around *euro*1 billion of much-needed capital. HVB thinks investors will be more interested in its operations in Austria and central Europe, which Bank Austria runs, than in the rest of its portfolio, which includes *euro*14 billion of non-performing loans. Does the sale make strategic sense, or is it just a desperate bid to prop up HVB's credit rating?

Probably the latter. If this is strategy, it is a swift about-turn: HVB bought Bank Austria only three years ago. Rated AA- in 1998, HVB has since seen its grade slip to A-. That has probably cost it an extra one-third of a percentage point on its funding, plus extra collateral to allow its trading counterparties to sleep more easily. Rating analysts say HVB would have been downgraded again but for this week's sale.

Indeed, the bank has rarely been on an even keel since its creation in a merger in 1997 of two Bavarian banks, both with huge mortgage books and a concentration of local corporate loans. At first the deal looked good, just the sort of merger that overbanked Germany still needs. “We're the only ones who consolidated,” says Dieter Rampl, the executive chairman.

But the deal went sour once the extent of one partner's over-optimistic property lending in eastern Germany came out. Mr Rampl wants to reduce HVB's risk-based assets by *euro*100 billion. Property loans amounting to over half that have been devolved to a new entity, HVB Real Estate Bank, which may in time be sold. To be commercially attractive, though, its rating needs to be at least A, not today's BBB.

In addition, HVB has set up a reinsurance operation in Bermuda, called Grand Central Re, that will manage around $10 billion of loans and mortgage-backed securities for HVB. It works like this: HVB lends $500m of “capital” to Grand Central Re. Grand Central leverages that capital to buy a portfolio of mortgage-backed securities and hedge-fund assets, most of it from HVB. The Bermudian firm must be prudent enough to maintain a decent credit rating: A.M. Best, which rates insurance companies, grades it A. The amount of regulatory capital HVB puts aside for this is a mere $40m.

Still more fancy footwork may be needed to improve HVB's reputation with shareholders and rating agencies. Germany's lacklustre economy is against it, as is the country's mortgage market, in which HVB would like to reduce its share. It is already selling repackaged loans to investors and will join other big German banks in securitising more. It wants to sell Noris Bank, a consumer bank based in Nuremberg, by the end of the month, and perhaps Vereins- und Westbank, in Hamburg; also Direkt Anlage Bank, HVB's online arm.

When HVB has managed all this, little will remain but a south German corporate and consumer bank, with a reduced share in its best asset, Bank Austria. Mr Rampl, sitting in his office in Munich, sees things differently: “I have a market share of 15% in south Germany, 25% in Austria and 15-21% in eastern Europe,” he says. All he needs is a stronger capital base.

Those who bought Bank Austria shares—which fell a little on their first day of trading—will be getting a slice of HVB's best division. It has consistently outperformed the group: Bank Austria's return on equity was 6.5% last year and 8.9% in the first quarter of 2003, against a negative return for HVB as a whole. On the other hand, some of Bank Austria's returns have come from such volatile areas as investments in hedge funds and trading cash, foreign exchange and derivatives for the bank's own account. Moreover, Bank Austria relies on business from HVB's German corporate clients. Now the dealing rooms of HVB and Bank Austria are to be split, giving less opportunity for such trading.

In its domestic market, Bank Austria is number one. Yet like Germany, Austria is one of the most overbanked markets in Europe: net interest margins have languished below 1.3% for the past six years. In central Europe, Bank Austria has perhaps the best coverage of any bank, certainly in the corporate market. But it has a strong retail presence only in Poland, through BPH, and Bulgaria, through Bank Biochim. Its Austrian rival, Erste Bank, thinks that retail banking is the main source of profit in the region, and so has bought retail banks with market shares of around 20% in the Czech Republic and Slovakia.

Bank Austria has tried to push into retail banking in Hungary and the Czech Republic, but with little success. It is bidding against Erste and others for Postabank, the last big bank for sale in Hungary. This week's share sale will give Bank Austria something to spend in central Europe, even though *euro*400m of it was earmarked for the purchase of the 18% of BPH that is still owned by HVB.

In any event, with 75%, the Bavarians still have control of Bank Austria, although remerger (or demerger) would require a 90% vote. If Bank Austria thrives, HVB's shareholders might indeed like to reclaim their full ownership in a few years, especially if in the meanwhile HVB has itself been acquired.

Yet the Austrian bank seems to have an instinct for survival. Its Creditanstalt part was saved by the government back in 1931, before being absorbed by Bank Austria in 1997. Now it has managed a partial escape from German hands. Although it is still Austrian by name, with this week's listing in Vienna it has regained some of its Austrian nature.

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Development

Years of plenty?

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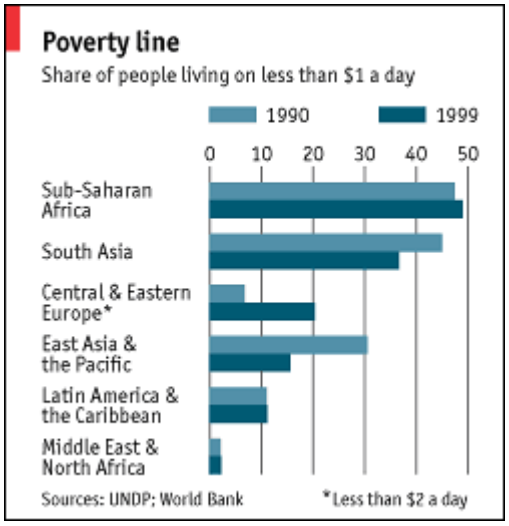
From The Economist print edition

The UN laments the 1990s

IN RECENT years the "Human Development Report", published by the United Nations Development Programme (UNDP), has stressed the importance of good governance and strong institutions in fostering economic growth. In 2002 the report espoused democracy. This year's effort, published on July 8th, concludes that governance and democracy, even together, are not enough.



In the 1990s, says the report, income per head fell in no fewer than 54 developing countries, even though these years were celebrated as times of reform and hope—and, in richer parts of the world, prosperity. The Human Development Index—a statistic summarising health, longevity, education and standards of living—fell in 21 countries during the decade, mainly as a result of the effect of AIDS on life expectancy. In the 1980s, the index fell in only four countries.

Not surprisingly, the countries that suffered most are in sub-Saharan Africa (although living standards in some former communist countries in eastern Europe and central Asia also fell). Most worrying is that it happened despite moves towards democracy and liberalisation in several African countries.

Why? "Location, location, location" is one explanation, says Mark Malloch Brown, head of the UNDP. Look at Uganda, lauded as an example for others to follow in the past decade. Despite GDP growth averaging over 6% in the previous ten years, Uganda's income per head was still less than $250 in 2001. Geography is a key constraint: Uganda is landlocked and has high transport costs. For similar reasons, the report finds that growth in China's southern coastal regions is five times that in the inland north-east.

Yet there are other reasons for the plight of poor countries, which have much to do with policy. Many have not diversified their economies away from commodities or done enough to foster small firms. Women are often marginalised. The report calls for substantial public investment in social and physical infrastructure to remedy these problems. This is likelier to help rapidly growing economies with large domestic markets, such as China and India, than a small African country dependent on stingy donors. The UNDP says that, if aid budgets remain tight, the proportion of people in sub-Saharan Africa living on less than $1 a day will not be cut by half until the middle of the 22nd century.

One lesson from the 1990s is that poor countries must take more responsibility for their own progress, by reducing their reliance on foreign investment and encouraging local capital formation. The lesson for the rich world is that it has an obligation to help. Sadly, it has not done enough. Although (promised) aid is on the rise again, between 1990 and 2001 aid from the 23 members of the OECD's Development Assistance Committee fell from 0.33% to 0.22% of GDP, compared with the 0.7% target set in 1970. Even better than more aid would be sincere trade liberalisation. It would be a start if the Doha "development" round of world trade talks began to live up to its name.

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About sponsorship

Wall Street research

Shortage of prophets

Jul 10th 2003 | NEW YORK
From The Economist print edition

America's equity research may be the best in the world. Big deal

FOLLOWING the long investigations and the terrible press, it sounds incredible. Yet a study by two business-school academics* concludes that equity-research analysts in America do a half-decent job—better than their counterparts in other markets. Second place goes to Japan, another country whose stockpickers are often disparaged. And the rest? Nowhere.

The study covers the period from October 1993 to June 2002, which saw a bull market, a bubble and a crash—an entire, explosive cycle. It includes all companies in the G7 economies whose shares met minimum requirements (eg, a price above $1 and coverage by at least one analyst who revised his opinion). Only in Italy, where the study ends in 1997, did the authors have problems collecting enough data. Maybe they gave up in despair, having concluded that Italian equity research was useless anyway.

The authors, Narasimhan Jegadeesh, of the Goizueta Business School at Emory University, and Woojin Kim, of the University of Illinois at Urbana-Champaign, calculated returns from the change in prices after analysts changed their recommendations. They tracked prices over five periods, ranging from one day to six months. In Italy, the initial impact of a change in recommendation was nil. Worse, over six months stocks receiving positive recommendations fell marginally in price not only in Italy but also in France, Germany and Canada. In all these countries research did provide value when advising customers to bail out.

Nothing in the study explains why research should have so little relevance in these markets. In Italy, especially, it may have something to do with the dominance of many listed companies by insiders with large, controlling blocks of shares. In some countries, it may also reflect the reliance of companies on banks, rather than capital markets, for finance. Market opinion simply matters less than in America.

In America, however, analysts' opinions do seem to have affected prices immediately: they rose by 1.8%, on average after an upgrade and fell by 3.2% after a downgrade. Over six months, the effects rose to 4.7% for buys and 6.3% for sells. The same general picture was true in Japan, although to a lesser degree.

Although equity analysis has been more successful in America, public anger about its failures has been more intense there than anywhere else. Mr Jegadeesh concludes that, since the anger cannot be explained by the data, it must stem from disappointed expectations. The industry may also have suffered from its reluctance to recommend selling. In America, sells comprised only 3.5% of recommendations covered by the study, and the rate declined steadily during the bull market. Elsewhere, the rate was 16%. Recently, says Mr Jegadeesh, this imbalance has ended.

Initially, Mr Jegadeesh suspected that, because American analysts have greater access to management and operate with more resources, the capital market would be more efficient than in other countries, so that analysts' opinions would have less impact. Yet this proved incorrect. Mr Jegadeesh believes recent changes in American securities regulations to eliminate conflicts of interest in equity research will have little impact. In countries where these conflicts are less severe, performance has been worse than in America.

For casual investors, the surprise may be that returns from following advice anywhere are so meagre. There are two reasons commonly offered for this. The first, which rings true, is that it is difficult to beat the market. The second defies statistical analysis, but also sounds likely: those who know where stock prices will go make use of the information themselves. It is only those who cannot make money from their research who sell it. The surprise is that there is value in any research at all.

* “Value of Analyst Recommendations: International Evidence”, by Narasimhan Jegadeesh and Woojin Kim

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About sponsorship

Asbestos litigation

Hatched, but not despatched

Jul 10th 2003
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Grumbles about America's proposed asbestos-compensation law

AP

After the litigation ends, the disease continues

FOR months Orrin Hatch, a Republican from Utah who is chairman of the Senate Judiciary Committee, has been negotiating an end to litigation over asbestos, scourge of both physical health and, via lawsuits, the financial health of America's insurers. On July 10th, after *The Economist* had gone to press, Mr Hatch's committee was due to vote on his draft bill. It proposes to establish a federal trust fund to last 27 years, out of which victims of asbestos would be compensated. The amount would depend on how sick they were.

Mr Hatch hopes his bill will become law by the end of the year. If it does, it should limit the costs to American business and insurers of asbestos claims, which in recent years have run out of control. So far, litigation has cost corporate America about $54 billion. If nothing is done, another $210 billion might be added on top, says the RAND Institute of Civil Justice, a think-tank in California. One-third of the 600,000 suits filed since the first, in 1966, are still pending. About two-thirds of the total have been brought by the “worried well”—people who are not ill, but think that they might be one day because of past exposure to asbestos.

Although a limit to all this may be in sight, insurers remain far from happy with Mr Hatch's plan. They say it will cost too much and will not, after all, put an end to uncertainty about what they will eventually have to pay. On July 3rd the American Insurance Association (AIA), a lobby group, wrote to Mr Hatch to express its “serious concerns”. It said it would oppose his bill unless the prospective cost is reduced to the level written into an earlier draft.

Mr Hatch's bill fixes ten different medical criteria, ranging from mesothelioma, a form of lung cancer, and asbestosis, a progressive scarring of lung tissue, through to shadows on X-rays. Insurers consider some of these too generous, such as a new category, “mixed causation”, created for people whose illness has uncertain causes that could include asbestos. “This makes the fund a magnet for new claims,” says Julie Rochman of the AIA.

Mr Hatch's first draft said that insurers and companies would each pay $45 billion into the $108 billion fund. The rest would come from the trusts of companies bankrupted by asbestos. However, Mr Hatch accepted a Democratic amendment to make insurers and businesses pay another $45 billion, increasing the size of the fund to $153 billion. They may be required to pay $2 billion a year even after their

contributions are supposed to end in 27 years' time, if there is no money left in the kitty. Democrats have also got Mr Hatch to accept that the maximum award for mesothelioma sufferers should be $1.1m, compared with the $750,000 first proposed.

Despite their public misgivings, insurers consider the bill to be better than none at all. Privately, they admit they had feared paying much more for asbestos compensation than even the amended text proposes. Business may also be relieved. One controversial beneficiary would be Halliburton, the energy group formerly run by Vice-President Dick Cheney.

Insurers note that the bill has the great merit of sidelining the lawyers: until now 40 cents of every dollar spent on compensation has gone in legal fees. No wonder the Association of Trial Lawyers of America (ATLA) is stepping up its fight against the bill. It claims that, if it is passed, defendants and their insurers “will laugh all the way to the bank.” Yet the lawyers have little sympathy from anybody except Democrats who depend on the ATLA's campaign cash. As Hank Greenberg, head of American International Group—AIG—the world's biggest insurer, put it, “The only people not benefiting from the Hatch bill would be the trial bar, and that, of course, would make us all very sad.”

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Economics focus

The euro, trade and growth

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From The Economist print edition

Do not expect a miracle

EUROPE'S single-currency area is in the mire. The German economy, which accounts for almost one-third of the region's output, is shrinking. Growth forecasts across the euro area are tumbling, in part because the euro has risen against the dollar. Meanwhile, the European Central Bank has been slow to cut interest rates, and the stability-and-growth pact, which restricts fiscal policy, is at best a joke, at worst an ordeal. You might suppose all this to be more than enough to test the faith of believers in the wisdom of the single currency.

Oddly, that faith is burning as brightly as ever. Despite the euro area's weak performance, enthusiasts are still expecting higher growth in the long run, because they think trade within the single-currency area will explode. The source of their confidence is an empirical finding from research into earlier currency unions. In this research, published in 2000, Andrew Rose, an economist at the University of California, Berkeley, extended the “gravity” model of trade. The idea, by analogy with Newton's theory of the gravitational pull of planets, is that trade between two countries increases with their economic size, but decreases with the distance between them (and therefore transport costs). Mr Rose's innovation was to add membership of a currency union as a possible influence on trade. Remarkably, he found that members of such unions trade three times as much with one another as do countries outside unions.

To many economists, this effect looked implausibly large. Currency unions should boost internal trade because companies and individuals no longer incur costs for changing money and because uncertainty about exchange rates within the union is eliminated. That said, the costs of currency transactions are small, and previous research has established that exchange-rate volatility reduces trade only marginally.

The critics questioned whether the research had allowed sufficiently for other factors likely to be associated with currency unions that would also generate higher trade volumes. These might simply reflect historical ties between countries. Leaving them out would exaggerate the estimates of the effect on trade of currency-union membership. In any case, because currency unions before the euro mainly linked small, poor countries, research into them was of little relevance to the euro area.

Subsequent research by Mr Rose and others has sought to overcome these objections. The general conclusion has confirmed that currency unions boost trade, but tempered the order of magnitude. A recent review of the evidence by the British Treasury concluded that joining the single currency would eventually boost Britain's trade with the euro area by between 5% and 50%, without diverting trade from non-euro countries.

As the range in this forecast suggests, doubts remain. The ending in 1979 of the currency union between Britain and Ireland seems not to have reduced trade across the Irish Sea. At first sight, the results from the euro area do not look encouraging, moreover. Trade within the euro area as a proportion of total trade fell in the three years to 2001. However, special factors are largely to blame: first America's boom and then rising oil prices lifted the proportion of trade with countries outside the zone. More detailed research suggests that the single currency is increasing trade among its 12 member states. The Treasury's best guess is that the long-run effect on trade of British membership would be towards the top of its 5-50% range.

Even if euro enthusiasts are right to expect a substantial increase in trade, they may be overstating its impact on growth. Gordon Brown, the chancellor of the exchequer, has told Parliament that a 50% increase in trade could raise living standards by almost 10% over the next 30 years. That is equivalent to an increase in Britain's potential growth rate over the same period of 0.3 percentage points a year, an

impressive effect.

Meanwhile, on the back of another envelope

However, the Treasury's economists also calculated that the gain in living standards might be only half that. The reason is that the greatest gains in living standards are reaped when economies first open up to trade. But after more than four decades of economic integration, culminating (one day) in a single market, European economies already trade intensively with each other. They are therefore likely to experience diminishing returns, in terms of economic growth, from further increases in trade.

Increased trade may also mitigate the biggest drawback of a currency union: the imposition of a single interest rate on diverse economies. As members trade more among themselves, their economic structures may become more alike: a large proportion of trade is between firms in the same industry. This may enable them to cope better with a common interest rate. Although a single interest rate makes national output more volatile, increased trade could dampen the impact. Alas, a contrary effect is also at work. One of the chief gains from a currency union may involve greater specialisation: Detroit as the centre of American carmaking, for example. But that would mean that economies got richer by becoming less, not more, alike. The recent collapse in the information-technology industry hit Finland and Ireland, which both have big IT sectors, hard.

It is plausible to argue that a single currency will boost trade and growth in the long run, offsetting the strains implied by a single interest rate. But the net benefits depend on much else besides. For a start, European countries have to be readier to pursue economic reforms. Bad policies, such as job-destroying regulations, could vitiate the potential gains from a single currency, just as they have limited the benefits from the single market. So could the stability-and-growth pact, by curbing governments' room for manoeuvre, which is already cramped by their decision to give up monetary policy to the ECB.

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Deep-vein thrombosis

Causing trouble

Jul 10th 2003
From The Economist print edition

Does air travel cause dangerous blood clots? If so, how? And who is responsible?

ONE of life's quietly satisfying moments is boarding a long-haul flight and turning left. Although air travel has lost much of its glamour, flying first or business class is still a relief to the senses, compared with the rigours of economy further aft. The space and relative quiet at the front of the plane certainly make flying a more pleasant experience, but do they make it any safer?

At issue is travel-related deep-vein thrombosis (DVT), otherwise known as economy-class syndrome. DVT describes the formation of clots known as thrombi in the blood vessels of various parts of the body, such as the lower leg. Clotting is a normal response to injury, and the body is continuously forming and removing clots that cause no obvious harm. Abnormal formation of clots, however, can lead to cramps, pain and swelling in the tissue affected. Far more serious is the possibility that the clot, or a piece of it, splits off and starts racing round the circulatory system. If this breakaway clot, called an embolus, gets stuck in a delicate part of the body, such as the lungs, it can kill.

Since the 1950s, doctors have documented cases of patients with a history of air travel also developing DVT. More recently, there have been dramatic cases of passengers dropping dead once off the flight. Journalists—who spend a lot of time on aeroplanes but rarely, alas, in business or first class—have been quick to pin the blame on the mile-high stuffy, cramped, immobile and dehydrating conditions of the “cattle compartment”.

Yet an association between flying and DVT does not necessarily mean that the one causes the other. Perhaps those who come down with DVT after travel already had the problem, undiagnosed, before they stepped on board? Pinning down the nature of any link requires large numbers of passengers and thorough testing both before and after they fly.

A rich vein of dispute

Barry Jacobson and his colleagues at the University of Witwatersrand in South Africa, and Guy's, King's and St Thomas's School of Medicine in London, have tried to do just that, in an attempt to see if passengers in economy class are more prone to DVT than those flying business class. In the latest issue

of the *South African Medical Journal*, they publish their findings on 899 passengers who have taken the 11-hour flight between Johannesburg and London. Passengers with a high risk of DVT—those, for example, who have recently undergone surgery, who have cancer, or who have a family history of the disorder—were excluded. The rest had blood samples taken when they got on the plane, to test for their levels of D-dimer, a molecule associated with clot formation. During the flight, they were asked to fill in a questionnaire about factors that might be associated with clotting: their fluid and alcohol consumption, exercise, smoking habits and medication. On arrival, more blood was taken to test for D-dimers, and half the passengers had their legs scanned by ultrasound, which can detect the narrowing of blood vessels caused by thrombi.

The results are controversial. None of the passengers scanned in either business or economy class had thrombi detectable by ultrasound. Good news for airlines keen to decouple flying and DVT? No, say the researchers. This is because roughly 10% of the passengers they studied developed elevated D-dimer levels during the flight, high enough to worry Dr Jacobson. Surprisingly, this did not depend on the class in which passengers travelled, the amount of fluid or alcohol they consumed, whether they smoked or whether they took sleeping tablets (thereby reducing their mobility). Raised D-dimer levels were, however, more common among those with a particular, inherited, form of a biochemical called Factor V Leiden, which is involved in clot formation. They were also high in those taking aspirin which, counterintuitively, is often prescribed to reduce clot formation and thus prevent heart attacks.

The South African findings are broadly consistent with recent results from another investigation called the New Zealand Air Travellers Thrombosis Study. This was led by Rodney Hughes, who now works at the Freeman Hospital in Newcastle-upon-Tyne, England. Among the 877 subjects of this study, 12% had elevated D-dimer levels after travelling in economy class for more than four hours. Roughly 1% of these were found to have either DVT or lung emboli, although none went on to develop serious complications.

However, the South African study, with its absence of detectable thrombi, is at odds with other research that shows a higher frequency of air-travel-related DVT. A series of studies carried out by Gianni Belcaro at the G. d'Annunzio University in Pescara, Italy, and his colleagues, suggest that low- to medium-risk passengers have a 1-4% chance of developing DVT from a flight, and that high-risk passengers have up to a 10% chance of coming down with it. Dr Belcaro has been looking at possible protective measures for high-risk passengers. He finds that injections of heparin, an anti-clotting agent, or the use of flight stockings, which keep blood circulating in the legs, can help to reduce the incidence of DVT in these passengers.

This whole area of research is fraught with trouble. To begin with, there is academic sniping: Dr Belcaro is sharply critical of the methods used by Dr Jacobson's group, and they in turn raise questions about Dr Belcaro's techniques. So, although many researchers agree that air travel affects the body's biochemically complex clotting system, but that the chances of an “average” passenger—that is, one without a pronounced risk of DVT on the ground—actually developing thrombi from air travel is small, the precise frequency of such thrombi is still fiercely debated. And nobody knows exactly what the trigger might be or how it is translated biochemically into a clot.

To tackle some of these questions, the World Health Organisation is trying to get an international study with thousands of passengers off the ground. But it will not be easy, says Dr Jacobson. Besides various technical problems, such as getting enough standardised equipment to different airports, persuading grumpy passengers trundling off a long-haul flight to hang around for testing is hard, even when they are rewarded with air miles, as they were in the South African study.

The clot thickens

And then there are commercial interests at stake. Carriers are keen to play down the whole notion of air-travel-related DVT. Some do, of course, hedge their bets by recommending that passengers drink lots of fluids and twiddle their toes, but there is not enough scientific evidence to know whether this makes a difference. On the other side drug companies, stocking manufacturers and medical-device makers stand to make money if air-related DVT takes off, as it were. Many of the academic studies in this field are partly supported by companies, so the results are often dogged by claims of conflicts of interest.

And as always, there are the lawyers to consider. So far, few of the lawsuits lodged by passengers against airlines, holding them responsible for DVT, have made much headway. That is because of a wrinkle in international law, according to John Goetz, a lawyer with Jones Day in Pittsburgh. Last week, for example, the English Court of Appeal turned down an attempt by 24 passengers to sue 18 airlines.

The judges maintained that the Warsaw Convention, which governs the liability of airlines flying internationally, does not permit their suits. But in the same week, in California, a federal judge allowed a case to vault over the hurdle of the Warsaw Convention, and inch a little closer to trial. If it gets its day in court, field studies looking at DVT and air travel will be important evidence, but, given the current state of disagreement, far from conclusive.

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DVDs

This movie will self-destruct

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A new twist on an old polymer

Time's up, Mr Phelps

EVERY time Jim Phelps, the leader of the “Mission: Impossible” team, picked up pre-recorded details of his latest assignment, he was told: “This tape will self-destruct in five seconds.” And lo-and-behold, with a puff of smoke, the tape turned to cinders. In August, fact will follow fiction with the arrival of the first real-life self-destructing recording medium. This has been made possible by tinkering with the molecular structure of a plastic that is even older than the television series.

Since 1966, when the first “Mission: Impossible” was broadcast, tapes have become old hat. The medium *du jour* is the DVD, and it is a self-destructing DVD that Buena Vista Home Entertainment, a division of Disney, plans to test-market in America next month. This DVD, known as EZ-D to its makers, Flexplay Technologies, of New York, can be played for 48 hours after being removed from its cover. It will then self-destruct—not in flames, its inventors hasten to add, but because contact with the air eventually renders its surface opaque, making it impossible for the laser in a disc player to read the data beneath.

There is method in this apparently mad product. The idea is to revamp the video-rental market. At the moment, if you want to hire a movie for a couple of days you have to pay $5 or so for a videotape or DVD that may well be a bit scratched by previous use, and then go to all the hassle of returning it to the shop when you have finished with it. And you have to watch it soon after you have hired it, or risk paying a fine. None of this, except the 48-hour viewing period, applies to an EZ-D. It will stay in pristine condition in its case for a year, and once it has been watched—as many times as you like within the two-day window—it can be thrown away. Or used as a beer mat, strung up with others as a bird-scarer or sent to a recycling scheme.

Flexplay developed the EZ-D in collaboration with the plastics division of General Electric (GE). The firm used a specially tweaked version of Lexan, a polycarbonate plastic that was stumbled upon in 1953 by Daniel Fox, a chemist who worked for GE. He noticed that the goo left behind in a beaker after one of his experiments had hardened into a tough polymer. Lexan has since become ubiquitous. It can be found in car panels, computer cases and even astronauts' visors, as well as in ordinary CDs and DVDs.

The original version of Lexan consists of chains of a single type of small molecule (a so-called monomer) linked together by a particular sort of chemical bond. The polycarbonate used in the EZ-D, by contrast, is a type known as a co-polymer, in which two different monomers form alternating links of the chain (though the bond remains the same). At the moment, GE is reluctant to go into detail about which monomers are involved, and how exposure to the air causes the colour change—although variations in the rate at which oxygen penetrates the co-polymer are a critical part of the process.

According to John Dineen, a vice-president at GE who is in charge of Lexan, the manufacturing process can be tweaked so that a disc remains playable for periods longer or shorter than 48 hours. This means EZ-Ds could be used for quick promotions such as movie previews, or for longer ones, such as when somebody is testing a computer-game. They could also be sold in new ways: to hotel guests, for example, or as “extra toppings” by pizza-delivery companies.

Bob Chapek, president of Buena Vista Home Entertainment, says that the first movies in the trial will include “The Recruit”, “The Hot Chick” and “Signs”. No sign, so far though, of a self-destructing “Mission:

Impossible”.

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About sponsorship

Detecting malingerers

Hidden truths

Jul 10th 2003
From The Economist print edition

It is now possible to distinguish those with real paralysis from fakers

A PATIENT visits his doctor to complain of a paralysed leg. The doctor performs a battery of tests but finds nothing physically wrong with him. He considers the possibility that the cause is psychological—a so-called conversion disorder or “hysterical paralysis” that has its roots in mental or emotional trauma, and refers the patient to a psychiatrist. But there is another possibility: that the patient is faking it. With only his patient's word to go on, a doctor's chances of distinguishing a malingerer from somebody with a real psychological illness are slim. A new brain-imaging test may, however, change that.

Nick Ward, of University College, London, and his colleagues, have found a marked difference between the pattern of brain activity displayed by a person pretending to be unable to move a leg, and that displayed by the same person when he is genuinely unable to move his leg. They believe these differences could form the basis of a test that would root out malingerers making false claims for compensation, care or time off work.

There is a wrinkle, of course. It was impossible to perform the experiment on people actually suffering from hysterical paralysis, since they would not be able to pretend they were malingering. So both paralysis and deception had to be induced in healthy volunteers under hypnosis. A dozen men, chosen because psychometric testing suggested they were highly suggestible, were hypnotised. They were then told either that they were unable to move their left leg in time with a metronome, or that they had to convince a white-coated observer that they were unable to do so—even though they themselves knew there was nothing wrong. Each subject was hypnotised first one way and then the other. And each time, snapshots of the subject's brain activity were taken using positron emission tomography.

The uniformed observer, who did not know which subjects were feigning and which were not, performed various neurological tests on the men, and monitored the activity of their leg muscles with electrodes stuck to their skin. He failed to distinguish the two groups. The brain scans, however, showed striking and reproducible differences between the two cases.

Those hypnotised into believing they were paralysed showed similar patterns of brain activity to patients with genuine conversion disorders whom the researchers had scanned in an earlier study. While brain regions that are involved in the preparation or imagination of a movement—a so-called motor response—were active, those involved in initiating movement were quiet. According to Peter Halligan, a psychologist on the team, this suggests that the subjects were not simply choosing not to move; they were genuinely unable to do so. In those feigning, by contrast, the researchers saw increased activity in brain areas associated with conscious planning—in particular the pre-frontal cortex. That suggests the subjects were consciously inhibiting a motor response. These “malingerers” showed the same activation of movement-preparation areas as did their “paralysed” counterparts, but the conscious-planning areas then kicked in to stop the movement from actually being performed.

Dr Halligan thinks the technique represents an improvement on traditional lie-detection methods that rely on monitoring changes in the skin's electrical resistance caused by perspiration. That is because it measures the brain's actual response to deception, rather than the physiological concomitants of that response. And he believes that, as the number of medically recognised conditions for which diagnosis rests almost exclusively on a patient's say-so increases—post-traumatic stress disorder for example—the opportunities for malingerers will multiply. Consequently, there will be a greater need for such a test, to protect the genuinely ill.

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The space shuttle accident

Foam alone

Jul 10th 2003
From The Economist print edition

Further evidence that a piece of insulation did it

Get article background

EPA

The hole truth?

SCIENTISTS like experiments. It is no surprise, then, to find that the investigation into the loss of the shuttle *Columbia* is following eerily similar lines to the investigation into the explosion of *Challenger* in 1986.

In that year, the cause of the accident was fixed in the public's mind after a dramatic public experiment by Richard Feynman, a Nobel prize-winning physicist. He dropped a piece of the shuttle called an “O-ring” into a cup of iced water to show how it failed at low temperatures. This time round, investigators have fired a piece of foam at a wing panel in order to simulate the action of a falling piece of foam that was seen to strike *Columbia* shortly after the shuttle took off.

This is the second such experiment. The first merely knocked loose a seal. This time, though, the drama of the event suggests another watershed moment in NASA history. “Oh my God!” one spectator is reported to have cried as the foam punched a hole about 40cm across into the panel.

Scott Hubbard, a member of the board investigating the accident, said the experiment showed that the foam was the most probable cause of the breach that led to the loss of *Columbia*. Gaps created in the protective shielding of the shuttle by the collision probably led superheated gases to breach the craft's left wing, causing it to disintegrate.

The board has already recommended that shuttle crew should be able to repair damaged wing tiles during a mission. But a hole of the size produced by the most recent experiment would be hard to mend. The board is now wrapping up its research and a final report is expected by the end of the month.

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About sponsorship

Mathematics

Riemann's riddle

Jul 10th 2003
From The Economist print edition

The oldest, most subtle and most difficult of unsolved mathematical problems is Riemann's hypothesis. Three new books explain its importance

WHEN Andrew Wiles, a British mathematician working at Princeton University, announced a decade ago that he had solved Fermat's last theorem, his discovery was reported on front pages around the world. The Frenchman's mathematical conundrum, which had taken more than 350 years to unravel, went on to inspire a television documentary, a bestselling book, and even “Fermat's Last Tango”—a musical that boasts such lines as: “Elliptical curves, modular forms, Shimura-Taniyama. It's all made up, it doesn't exist, algebraic melodrama.”

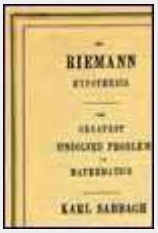
Three new books grapple with what is arguably an even tougher problem: the Riemann hypothesis, a puzzle that has perplexed mathematicians for the last century and a half.

Riemann's hypothesis is just 15 words: “The non-trivial zeros of the Riemann zeta function have real part equal to 1/2”. But explaining it so that non-mathematicians can understand it is more complicated. The distribution of prime numbers, such as 5, 7 and 11, does not follow any regular pattern but they become less common as they grow bigger. In an 1859 paper, Bernhard Riemann, a 33-year-old German mathematician, observed that the frequency of prime numbers is very closely related to the behaviour of an elaborate function, “ξ (s)”, which came to be named the Riemann zeta function.

The Riemann hypothesis asserts that all non-trivial solutions of the equation ξ (s) = 0 lie on a straight line. This has been checked for the first 100 billion zeros, but no proof appears to be in sight. The real significance of the hypothesis lies in its consequences, and particularly in what it says about prime numbers. A proof that held for every zero would shed new light on many of the mysteries surrounding the distribution of primes.

Mathematicians have been fascinated with prime numbers ever since the third century BC, when Euclid proved that there are an infinite number of them. Early

The Riemann Hypothesis: The Greatest Unsolved Problem in Mathematics
By Karl Sabbagh



Farrar, Straus and Giroux; 340 pages; $25

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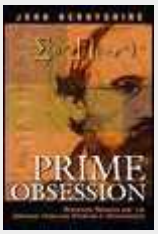
Prime Obsession: Bernhard Riemann and the Greatest Unsolved Problem in Mathematics
By John Derbyshire

in the 19th century, they began to look more closely at how often primes occur among the integers. Although Riemann, who died at the age of only 39, also laid the foundations in geometry for Einstein's general theory of relativity, his paper on prime sattracted little attention in the decades after it was first published.

A major breakthrough came in 1896, when two mathematicians independently proved the Prime Number theorem, which showed not just that prime numbers become rarer as they grow larger, but that their reoccurrence follows a specific formula (for those who care, the average gap between consecutive prime numbers is roughly proportional to the logarithm). The Prime Number theorem also encouraged mathematicians to begin working on Riemann's hypothesis, which gives a far more detailed picture of how the primes are distributed and which has consequences, not just for prime numbers, but also for many other areas of mathematics, including the analytic properties of L-functions and representations of non-singular cubic forms.

The fame of the Riemann hypothesis has grown steadily over the past 150 years. In 1900, David Hilbert, a German mathematician and contemporary of Einstein's, in a famous speech to the International Congress of Mathematicians, presented a list of what he considered to be the 23 most important problems for the new century. Hilbert's problems came from a variety of mathematical fields, and were to have a significant influence on 20th-century mathematics. One hundred years later, the Clay Mathematics Institute, which was founded by Landon T. Clay, a Boston businessman, published its list of what it called the seven millennium-prize problems, and promised a $1m reward for solving any one of them. The Riemann hypothesis appears on both lists.

Riemann's riddle has become a fixture on the mathematical landscape. Over the years, hundreds of results have been published that assume the truth of the hypothesis, but a proof of the conjecture would have immense consequences. Equally, a disproof would be the mathematical equivalent of an earthquake, destroying decades of work at a stroke.



Joseph Henry Press; 448 pages; $27.95

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The Music of the Primes: Searching to Solve the Greatest Mystery in Mathematics
By Marcus du Sautoy

HarperCollins; 352 pages; $24.95. Fourth Estate; £18.99

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All three of these books offer fascinating accounts of the story surrounding the Riemann hypothesis. Karl Sabbagh approaches the subject in the manner of an anthropologist, recording dozens of conversations with mathematicians working on various aspects of the problem. As a non-mathematician, he appreciates the difficulty of explaining a recondite mathematical problem to a general audience, and gives a vivid account both of the passion that mathematicians have for their subject and of the fascination for this particular problem.

John Derbyshire's book is more of a historical adventure. Chapters alternate between broad-scale historical accounts and detailed mathematical presentation. Some readers may find the mathematical chapters heavy going, but Mr Derbyshire makes a valiant attempt at explaining the mathematical ideas around the problem. His historical chapters link mathematical developments to the lives and personalities of the mathematicians involved and are full of interesting stories.

The most detailed account is given by Marcus du Sautoy. A professor of mathematics at Oxford University, Mr du Sautoy provides an engaging and accessible history of work on prime numbers and the Riemann hypothesis. He also has an eye for modern applications, and offers detailed discussion of the relevance of the Riemann hypothesis to cryptographic security as well as an interesting account of its possible links with quantum physics.

What, then, are the prospects that the hypothesis will ever be proved? In the 18th century, Leonhard Euler suggested that the distribution of prime numbers could be “a mystery into which the human mind will never penetrate”. But, to judge from Mr Sabbagh's book, most mathematicians would incline more towards Hilbert's view that a solution will one day be found for even the most difficult mathematical problem. Hilbert's words, expressed in a speech he made in 1930, were carved on his tombstone after his death: *Wir müssen wissen. Wir werden wissen.* “We must know. We will know.”

The Riemann Hypothesis: The Greatest Unsolved Problem in Mathematics.
By Karl Sabbagh.
Farrar, Straus and Giroux; 340 pages; $25

Prime Obsession: Bernhard Riemann and the Greatest Unsolved Problem in Mathematics.
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The history of Japan

Tokyo rose

Jul 10th 2003
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ON FEBRUARY 11th 1889, the Meiji emperor, dressed for the occasion in a European field-marshal's uniform, took his seat on a Prussian armchair in a European-looking throne-room in the palace of his new capital, Tokyo. There, he announced the enactment of a new constitution, providing for Japan's first parliamentary elections. Japan, it was hoped, was taking its place among the world's great modern nations.

The granting of the constitution was meant to cap a turbulent period of 36 years since Commodore Perry's unopposed arrival, in his black naval ships, had graphically brought home to the Japanese how badly they had fallen behind. Now, with the shogunate abolished, the emperor restored to his supposed ancient authority, and an exhaustive programme of learning from the West (rather than, as in the past, from decrepit China) well under way, it was meant to be, as the term Meiji denotes, an Age of Brightness.

Inventing Japan 1853-1964
By Ian Buruma

Modern Library; 194 pages; $19.95. To be published in Britain by Weidenfeld & Nicolson in September

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And so it was, for a time. In 1905, Japan defeated Russia, to the astonishment of the world. Tokyo and other Japanese cities became thoroughly modern places, complete with cinemas, dance-halls and liberated young people. From the outset, though, there was a dark side. The constitution, like the throne, was largely Germanic, and played with deadly effect in a land already conditioned to Confucian worship of authority. The democracy it imported was largely a chimera—the franchise extremely restricted, the ministers appointed by the emperor, not parliament. Unfortunately, the militaristic element it brought was not. Between 1932 and 1945, Japan was to have 14 prime ministers, only four of them civilians. The war into which these soldiers led Japan left the country devastated, but it also gave it a chance to learn a new set of lessons from the West.

Ian Buruma's excellent new book charts the process of Japan's engagement with the western world from Perry's arrival to the Tokyo Olympics in 1964, at which point Japan might fairly be said to have arrived as a respectable member of the world community, having put firmly behind it the shame of the second world war and the ensuing American occupation. It is, of course, an arbitrary cut-off point, as the author himself agrees. Meaty questions remained then and still remain, not least the perennial debate over whether Japan should continue to shelter under America's military umbrella indefinitely, or develop a fully-functional military capability of its own. But Mr Buruma's chosen period, spanning just over a century, encapsulates neatly Japan's struggle to get out of China's shadow without falling completely under America's.

It makes for a compelling read. A striking aspect of the tale is the extraordinarily savage nature of Japan's political process during that time; the number of assassinations, and the bitterly factional nature of every institution from the court to the army are all powerfully depicted. Squeezed between right and left, as in Weimar Germany, Japanese democracy never had much of a chance.

There are good discussions, too, of how Japan could have come to commit an atrocity as grotesque as the Rape of Nanking (in which an estimated 250,000 people were killed during just six weeks in the winter of 1937), and of Douglas MacArthur's occupation—a time when censorship, carried out in the name of democratisation, was so extreme that one was forbidden to refer to the fact that there was any censorship. One disappointment is that Mr Buruma avoids giving a clear judgment on the central question of the extent of Emperor Hirohito's war guilt, and whether he should have been tried as a war criminal, rather than being allowed to remain on the throne.

Despite that, this slender volume packs in more information than you would be lucky to find in a book twice its size. It is beautifully produced, too. These are the hallmarks of Modern Library Chronicles, a new series which includes Richard Pipes on Communism, Bernard Lewis on the Holy Land and Chinua Achebe on Africa. If they are all as good as this, the books will be well worth collecting.

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German cinema

Auf Wiedersehen, pet

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How to make Germans laugh

IN THE nest of worker ants that peopled Erich Honecker's nasty regime there were living, loving humans who tried to make life bearable for each other. That is the focus of Wolfgang Becker's “Goodbye, Lenin!”, a film whose humour has succeeded in uniting east and west Germany in a way that no transfer of money or know-how has yet managed.

Alex's single parent, Mum, a staunch Honecker babe, has a heart attack and falls into a coma just before the collapse of the Berlin wall in 1989. When she wakes up eight months later, the doctor tells Alex and his sister that any outside shock could kill her. So they cocoon her in her familiar socialist world. They lovingly recreate her bedroom in Stalinist chic; they search rubbish heaps and empty apartments for once-cherished brands—ersatz coffee, flickering light bulbs, a Russian cassette/radio, whose aerial Alex breaks to block out unwanted news.

When Mum gets more curious, sees Coca-Cola adverts outside her window, and wants to watch TV, Alex and his West German friend Dennis shoot dummy East German newscasts. The newsreader (Dennis in shiny synthetic suit) explains that Coca-Cola was a socialist invention; that the thousands of people seen crossing the border are West Germans, fed up with the capitalist rat-race and wanting homes in the East. “Idiocy,” Mum concludes.

She may have smelled a rat. But she plays along; they all do, including the neighbours and children, who are paid to dress as Marxist Pioneers and sing patriotic songs, because the trip into *Ostalgie* (nostalgia for the East) has become a common obsession.

The socialist world that Alex and his friends recreate is an idealised one, in which Sigmund Jähn, the country's only cosmonaut, and one of its few popular heroes, becomes head of state. Adversity is met with stoicism. Mum's response to a mass-produced pullover that would only fit a fat dwarf is a long-suffering: “We in the German Democratic Republic must endeavour to become smaller and squarer.”

Alex is played by Daniel Brühl, a German heart-throb, with the face of a young Jeremy Irons and the eyes of Omar Sharif. The love that Alex shows for his mother, the understanding for his missing father who defected, the resilience of family and friends, have a quality that even strangers to recent German history can enjoy. At least that is what the distributors are counting on. The film is released in Britain this month and afterwards in America.

“Goodbye, Lenin!” was chosen as the best European film at this year's Berlin film festival and has won

nine other awards. It is the warmest souvenir yet of a nation that died almost overnight.

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European integration

A new hymn sheet

Jul 10th 2003
From The Economist print edition

THE question “what kind of Europe?” is both descriptive and prescriptive—as well as highly controversial. Eurosceptics believe that the European Union is becoming something close to a federal state, but would like it to be much more like a free-trade area. Federalists often argue that the EU is still primarily an economic organisation, but they would prefer to turn it into something more akin to a state.

What Kind of Europe?
By Loukas Tsoukalis

Oxford University Press; 240 pages; $35 and £25

Buy it at
Amazon.com
Amazon.co.uk

In the continuing debate about the nature and aims of the European Union, those who make clear and interesting arguments are often ill-informed; while those who are well-informed often write in the obscure and boring manner typical of EU insiders.

Loukas Tsoukalis manages to break out of this grim paradigm. As a Jean Monnet professor at the University of Athens and an occasional fellow of the Robert Schuman Centre for Advanced Studies and the Collège d'Europe, he is an EU insider par excellence. But, despite these disadvantages, he has still managed to write a book about the European Union which takes on big questions and writes about them in clear and lively language (although his use of brackets is excessive and distracting).

Mr Tsoukalis's central argument is that the traditional ways of looking at the European Union are becoming out-moded. He argues, accurately enough, that the central political question has usually been defined as whether there should be more or less political integration—a tug-of-war between “Brussels” and the nation-state. He also acknowledges that European integration has essentially been “mostly the product of an elite conspiracy, with good intentions and pretty remarkable results.”

In Mr Tsoukalis's view, however, both these central features need to change: “The elitist character of European integration has been rapidly reaching its limits. The European project needs to become more democratic and hence more explicitly political.” The definition of what “political” means also has to alter. Mr Tsoukalis would substitute an argument about the nation-state versus the European Union, with a pan-European politics focused on the kind of “left-right” choices that have up until now been largely argued out within national political systems. This would mean acknowledging that EU policies such as the single market and the single currency that have hitherto been presented as technocratic and politically-neutral are in fact highly political and create winners and losers.

The kind of Europe that Mr Tsoukalis would create would not be to everybody's taste. He would anger the French by cutting back the common agricultural policy and alarm the Spanish and the Poles by partially re-nationalising structural funds. He would enrage the British and the Irish by pushing for a European Union tax. And he would re-direct much of this money toward strengthening the EU's common foreign and immigration policies.

He would upset federalists by opposing the creation of a pan-European welfare state, but he would also irritate anti-federalists by pressing for an elected president of Europe. However, all sides in the argument about the future of the European Union would profit from reading his book, which manages to summarise old arguments in a succinct and accessible way, while also introducing stimulating new ideas to the debate.

What Kind of Europe?
By Loukas Tsoukalis.
Oxford University Press; 240 pages; $35 and £25

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About sponsorship

Thomas Jones

Perfection in miniature

Jul 10th 2003 | CARDIFF
From The Economist print edition

A modernist before his time

FEW painters enjoy as much renown per square inch as Thomas Jones (1742-1803). The fame of this Welsh landscapist, forgotten until recently, rests on roughly half a dozen small oil sketches of walls and rooftops in Naples, some of them no larger than a postcard. So modern are they in treatment and atmosphere that many people, seeing them for the first time, have trouble believing they were painted in Italy in the early 1780s.

The most famous, “A Wall in Naples”, has been called “one of the great microcosms of painting”. Though a detailed and beautiful depiction of what Jones might have seen from his hot upper window, the sketch has a flatness and all-over composition that would not have looked out of place among experiments in abstraction 150 years later.

These enigmatic gems are on show in the National Museum & Gallery, Cardiff, together with more conventional works, spanning the whole, on-off career of a sporadic genius. It is a fascinating exhibition, put together by Ann Sumner and Christopher Riopelle. In August it travels to Manchester and then London.

The second son of a Welsh landowner, Jones was bound for the church, but money for university ran out when a family patron died, and he turned instead to art. After studying under a landscapist, Richard Wilson, copying and learning to forge his teacher's work, Jones made the obligatory trip to Italy in 1776. He stayed seven years, filling his sketchbook with notations of the land and buildings of Rome and Naples. (You can view the book on a screen in the show.) Although Jones's lively and amusing “Memoirs” reveal him as no recluse, his drawings rarely show people, not even for scale. He was simply no good at, or not much interested in, depicting human form. Discerning eyes have nevertheless seen metaphors of the body in his Naples sketches, with their ambiguous openings and expressive façades.

Jones's formal originality lay in what he did to the picture plane. You will have seen hundreds of 17th- and 18th-century landscapes which draw your eye across a dark foreground to a luminous vanishing point as if looking through a window at an imaginary space. In the Naples sketches, the light falls evenly at the front, as on a curtain. Indeed there is virtually nothing but foreground, no vanishing point, and old-fashioned picture-space is abolished. Once Jones came to see the picture plane so flatly, devoting an entire picture to a wall must have felt perfectly natural.

Did Jones recognise his own originality? His memoir entries for the summer of 1782 are more about the heat and the rent. Commissions were few, and he seems to have felt himself a failure. On returning from

Italy, he inherited the family estate and painted only intermittently. Yet traces of his probing, experimental nature—the lighting of the foreground, the sharpening of transitions from light to dark, the all-over patterning—are there to see both before and after Naples. Some innovations come too early, others falter from lack of confidence or peter out through ill luck. With Jones it was probably all three. But a pathbreaker he undoubtedly was.

"Thomas Jones, An Artist Rediscovered" is at the National Museum & Gallery, Cardiff, until August 10th, before moving on to the Whitworth Art Gallery, Manchester, August 22nd-October 26th, and the National Gallery, London, November 12th 2003-February 15th 2004.

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About sponsorship

Political thriller

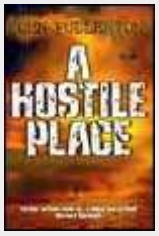
Kabul bounty

Jul 10th 2003
From The Economist print edition

ANYONE who is wondering what has happened to Osama bin Laden might enjoy taking this thriller to the beach.

Thomas Morgan, soldier, spy, thief and would-be rich man, is the hero of John Fullerton's second novel. Caught in a flawed attempt to “liberate” the silverware from the British embassy in Kabul, he is easily persuaded by the sinister Quilty and the beautiful Mathilde, both of the British secret service, to carry out a rather more tricky operation. At the head of a fairly identikit crew of international tough-guys, he is sent back into Afghanistan to assassinate “the Sheik”, return with physical evidence, preferably in the form of his head, and pick up a $25m bounty in the process. Without going into fun-wrecking detail, suffice it to say that Things Go Wrong, not least in the form of a minutely described attack of amoebic dysentery that should not be read immediately after breakfast.

A Hostile Place
By John Fullerton



Macmillan; 294 pages; £15.99

Buy it at
Amazon.co.uk

So far, so predictable. Where “A Hostile Place” manages to transcend its rather clunky writing—characters have an annoying habit of spelling out to each other, for the benefit of the reader, spiels about Afghanistan and al-Qaeda that all of them would obviously know backwards—is in the feel that the author has for his terrain. Mr Fullerton knows what he is talking about, having reported for the Reuters news agency from Afghanistan and Pakistan and lived for two years in Peshawar in the 1980s, when it was home to the *mujahideen* resistance. He gets the landscape right, and the people, with their curious mix of courtesy and savagery, right too.

But where the novel really scores is in its fundamental plausibility. If Mr bin Laden is still alive, rather than buried in a collapsed cave, this is exactly where he is most likely to be. Mr Fullerton makes you see just how difficult it would be for the Americans, for all their night-sights and image-intensifiers, SIGINT, ELINT and satellite photographs, to track a man down in such a landscape—especially one protected by the intricacies of kinship, shared battles and wealth.

He's capable of a biting line in cynicism, too. “Back then, the Soviets said they were fighting *basmachi*, bandits, backed by Pakistani intelligence and the CIA,” says Morgan at one point. “Today, the Americans say they are fighting terrorism. In many cases, they were the same people.” Too true, alas, too true—and the Sheik was one of them.

A Hostile Place.
By John Fullerton.
Macmillan; 294 pages; £15.99

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About sponsorship

Antonio Fortich

Jul 10th 2003
From The Economist print edition

Antonio Fortich, fighting bishop of the Philippines, died on July 2nd, aged 89

THE ceremonial opening of the Martial Law Museum in Manila in 1999 was carried out by Antonio Fortich, a bishop in the Roman Catholic church. He was handed wire-cutters and snipped through the barbed wire that was thought more appropriate to the occasion than a ribbon. Those who had suffered under the martial law regime of Ferdinand Marcos felt that the bishop had done as much as any public figure in the Philippines to oppose the dictatorship. More than that: the bishop, known to his supporters as Commander Tony, was still in fighting mood long after Marcos had been deposed. The museum conveyed a “sense of horror”, he said, but for millions of people in the Philippines their horrors had not ended when Marcos quit in 1986. The subsequent restoration of democracy had meant little to his own people in Negros.

Negros is a large island in the southern Philippines. Antonio Fortich was bishop of Bacolod, its main town. Negros has long been the sugar bowl of the country. From an aircraft you can see a vast stretch of green cane that covers much of the land. The United States expanded Negros's sugar industry when it took possession of the Philippines after defeating Spain in 1898, and continued to be its main export market after the Philippines gained independence in 1946. The landowning families of Negros, mostly of Spanish stock, became rich, providing welfare for their sugar workers in return for subservience. But America eventually developed its own sugar industry. In the 1980s the price of Philippine sugar crashed.

The sugar barons were no longer making money, and the welfare system for the workers was collapsing. Hundreds of children were dying of malnutrition. Bishop Fortich said that what was known as *tiempo muerto* (the dead season, after the sugar has been harvested) had expanded and become *tiempo del muerto* (a time of death). The island, he believed, could become a “social volcano”.

A sparrow's tale

The poor in Negros turn to the church or the communists. In its hunt for communists, the army made Negros an area of “low-intensity conflict”. Many communists were killed, but many innocent people died too, either because they were accused of helping the communists or because they were caught in crossfire. Bishop Fortich rushed to a church hall in Negros where 500 villagers were being threatened by army “death squads” and persuaded the soldiers to leave. He once showed reporters a dead sparrow he had found. The bird, he said, was just like any poor citizen caught in the crossfire of contending ideological forces. The bishop had the sparrow stuffed and mounted and kept it on his desk.

Bishop Fortich said he did not support any ideology. But in the Philippines, as in Latin America, not even a priest can escape politics. For many in authority priests are still considered to be as dangerous as in Graham Greene's “The Power and the Glory”. Bishop Fortich's superior, Cardinal Jaime Sin, archbishop of Manila, provides guidelines to his clergy: like the bishop, he thundered in the pulpit against the iniquities of Marcos, but granted him the blessings of the church.

Bishop Fortich probably stretched the guidelines. He spoke against the hanging judges of Manila who called themselves the Guillotine Club. He was one of the first people to alert the government to the activities of timber bandits who had stripped hundreds of acres of forest in Negros. He supported the election of Joseph Estrada as president of the Philippines; it was clear that he was the overwhelming choice of the ordinary people, sick of successive governments being run for the benefit of the rich. He

persuaded the president to release 200 political prisoners. It was only when it became clear that Mr Estrada had betrayed his supporters by lining his pockets that the bishop withdrew his support.

In keeping his flock together, he sought to show that the church was a better fighter for their interests than the communists. He said the sugar barons should be more generous to their workers. Cutting sugar cane, swinging a machete all day and loading lorries is a tough job, made worse in the suffocating heat by having to wear thick clothing to provide protection from the sharp leaves. After paying his employer for food a worker might be left with only a few pesos at the end of a month. To tide him over he would get in debt, which would grow year by year.

Bishop Fortich set up a co-operative composed of small landowners and sugar workers, to show what could be done. He wanted the great sugar estates broken up and land distributed to small farmers, who would grow other crops. The Philippines no longer exports sugar. To satisfy its sweet tooth, most years it imports some, at a price lower than the home-grown cane. The sugar barons accused the bishop of being a traitor to his class: after all, his parents had themselves been landowners in Negros. As a warning, a hand grenade was lobbed into his house in Bacolod.

He was nominated for a Nobel peace prize, praised by Pope John Paul II, and many of his followers thought of him as a saint. Cardinal Sin said that he was sure that, in heaven, the bishop would “intercede for us”.

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Overview

Jul 10th 2003
From The Economist print edition

American unemployment surged to 6.4% in June, up from 6.1% in May—far worse than most forecasters had expected.

Stockmarkets heated up, while bonds cooled. America's **NASDAQ** rose to its highest level in over a year. In Japan, the **Nikkei** index rose briefly above 10,000 for the first time since August. Reflecting the renewed interest in shares, ten-year bonds issued by the Japanese government saw yields rise above 1%, and yields on ten-year German government bonds touched 4.0%, their highest level in two months.

Germany's industrial output suffered a sharper than expected contraction of 0.7% in May, bringing industrial-production growth for the 12 months to May to a paltry 0.2%. On a positive note, the country experienced a surprise fall in unemployment. According to new figures, GDP in **France** grew by 1.1% in the year to the first quarter, up slightly from preliminary estimates.

The Dutch economy also did a bit better than earlier estimates: it grew by 0.2% in the year to the first quarter. Industrial production fell by 3.7% in the 12 months to May.

Britain's trade figures were revised to take account of a massive scam to avoid VAT. Imports for the four years 1999-2002 were deemed to be £22.7 billion ($34.5 billion) higher than previously reported.

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Output, demand and jobs

Jul 10th 2003
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2003	2004	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		Unemployment % rate year ago
Australia	+ 2.9	Q1	+ 2.8	+ 2.8	+ 3.5	nil	Q1	+ 4.0	Q1	6.1	Jun	6.5
Austria	+ 1.3	Q4	– 0.5	+ 0.5	+ 1.3	– 1.5	Dec	– 3.1	Mar	4.4	Jun	4.3
Belgium	+ 1.3	Q1	+ 0.6	+ 0.8	+ 1.6	– 3.8	May	nil	Apr	11.6	Jun†	10.4
Britain	+ 2.1	Q1	+ 0.3	+ 1.8	+ 2.5	– 2.6	May	+ 3.1	May	5.1	Apr††	5.2
Canada	+ 2.6	Q1	+ 2.4	+ 2.3	+ 3.0	– 1.0	Apr	+ 1.4	Apr	7.8	May	7.7
Denmark	+ 1.2	Q1	+ 1.4	+ 1.0	+ 2.0	– 0.8	May	– 1.6	Apr	6.0	May	5.1
France	+ 1.1	Q1	+ 1.1	+ 0.8	+ 1.9	– 0.5	Apr	– 2.0	May	9.3	May	8.9
Germany	+ 0.2	Q1	– 0.9	nil	+ 1.2	+ 0.2	May	+ 0.8	May	10.6	Jun§	9.8
Italy	+ 0.8	Q1	– 0.4	+ 0.6	+ 1.6	+ 1.7	Apr	+ 3.0	Apr‡	8.8	Apr	9.0
Japan	+ 2.6	Q1	+ 0.6	+ 0.8	+ 0.8	+ 1.6	May	– 2.3	May	5.4	May	5.4
Netherlands	+ 0.2	Q1	– 0.3	– 0.2	+ 1.3	– 3.7	May	– 0.6	Mar	5.3	May**	3.8
Spain	+ 2.1	Q1	+ 2.0	+ 1.9	+ 2.6	– 1.3	May	+ 2.7	Apr	11.3	May	11.2
Sweden	+ 2.2	Q1	+ 2.4	+ 1.4	+ 2.1	+ 3.4	Apr	+ 2.7	May	4.2	May†	3.4
Switzerland	nil	Q1	– 1.0	+ 0.1	+ 1.4	+ 0.9	Q1	– 5.9	Mar	3.6	Jun†‡	na
United States	+ 2.0	Q1	+ 1.4	+ 2.3	+ 3.4	– 0.8	May	+ 6.1	May	6.4	Jun	5.8
Euro area	+ 0.8	Q1	nil	+ 0.6	+ 1.7	+ 0.8	Apr	+ 2.2	Apr	8.8	May	8.3
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 1.2	Q1	– 4.9	na	na	– 1.5	May	+ 3.7	Mar	11.4	May†	11.9
Greece	+ 4.3	Q1	na	na	na	– 0.1	Apr	na		na		na
Iceland	+ 3.3	Q1	na	na	na	– 0.3	2002	na		3.6	May†	2.5
Ireland	+ 6.4	Q4	na	na	na	+ 3.7	Apr	+ 3.2	Apr	4.7	Jun	4.4
Luxembourg	+ 1.1	2002	na	na	na	+ 4.5	Mar	+ 4.6	Jan	3.6	May	2.7
New Zealand	+ 3.6	Q1	+ 3.3	na	na	+ 5.9	Q4	+ 6.4	Q1	5.0	Q1	5.3
Norway	+ 0.6	Q1	+ 1.3	na	na	– 5.7	May	+ 3.5	May	4.4	Q1	4.1
Portugal	– 1.2	Q1	+ 0.3	na	na	– 2.6	May	+ 0.3	May	6.4	Q1†	4.5

*% change at an annual rate. †Not seasonally adjusted. ‡New series. ††Feb-Apr; claimant count rate 3.1% in May. §EU harmonised rate 9.4% in June. **Mar-May.

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Prices and wages

Jul 10th 2003
From The Economist print edition

% change on year ago

	Consumer prices			The Economist poll consumer prices forecast		Producer prices			Wages/earnings		
	latest		year ago	2003	2004	latest		year ago	latest		year ago
Australia	+ 3.4	Q1	+ 2.9	+ 2.9	+ 2.5	+ 3.0	Q1	+ 0.5	+ 4.3	Q1	+ 4.1
Austria	+ 1.1	May	+ 1.9	+ 1.4	+ 1.1	+ 1.7	Jun	– 1.7	+ 2.1	May	+ 2.4
Belgium	+ 1.6	Jun	+ 0.9	+ 1.3	+ 1.1	– 0.4	May	– 0.2	+ 2.4	Q1	+ 3.1
Britain	+ 3.0	May	+ 1.1	+ 2.8	+ 2.4	+ 1.3	May	+ 0.1	+ 3.2	Apr	+ 3.3
Canada	+ 2.9	May	+ 1.0	+ 2.9	+ 2.0	– 1.7	May	– 2.2	+ 1.9	Apr	+ 2.8
Denmark	+ 2.2	Jun	+ 2.2	+ 2.3	+ 1.8	– 0.6	May	– 0.3	+ 3.9	Q1	+ 4.0
France	+ 1.8	May	+ 1.4	+ 1.8	+ 1.3	+ 0.7	May	– 1.2	+ 2.9	Q1	+ 4.0
Germany	+ 1.0	Jun	+ 1.0	+ 0.8	+ 0.5	– 0.2	May	– 1.3	+ 2.3	Apr	+ 2.4
Italy	+ 2.6	Jun	+ 2.2	+ 2.5	+ 1.8	+ 1.6	May	– 0.5	+ 1.7	May*	+ 2.3
Japan	– 0.2	May	– 0.9	– 0.4	– 0.5	– 1.0	May	– 2.2	+ 2.4	May	– 0.3
Netherlands	+ 2.2	Jun	+ 3.4	+ 2.4	+ 1.8	+ 2.5	May	– 1.9	+ 2.9	May	+ 3.6
Spain	+ 2.7	May	+ 3.6	+ 3.0	+ 2.5	+ 0.7	May	+ 0.5	+ 4.9	Q1	+ 4.0
Sweden	+ 1.9	May	+ 2.0	+ 2.1	+ 1.7	– 1.4	May	– 0.2	+ 2.3	Apr	+ 2.6
Switzerland	+ 0.5	Jun	+ 0.3	+ 0.7	+ 0.7	– 0.5	May	– 1.3	+ 1.8	2002	+ 2.5
United States	+ 2.1	May	+ 1.2	+ 2.2	+ 1.5	+ 2.5	May	– 2.9	+ 3.0	Jun	+ 2.8
Euro area	+ 2.0	Jun	+ 1.9	+ 1.8	+ 1.3	+ 1.3	May	– 0.8	+ 3.0	Q1	+ 3.3
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 0.7	May	+ 1.4	na	na	– 1.3	May	– 1.8	+ 4.1	Q1	+ 3.2
Greece	+ 3.8	Jun	+ 3.3	na	na	+ 2.4	May	+ 1.3	na		na
Iceland	+ 1.8	Jun	+ 4.8	na	na	+ 3.2	Jul	+ 7.1	+ 5.6	May	+ 7.5
Ireland	+ 3.7	May	+ 4.7	na	na	–10.0	May	– 0.5	+ 7.1	Q1	+ 6.9
Luxembourg	+ 1.8	Jun	+ 1.7	na	na	+ 1.8	Apr	– 2.5	+ 3.1	Mar	– 1.2
New Zealand	+ 2.5	Q1	+ 2.6	na	na	– 1.3	Q1	+ 2.8	+ 2.3	Q1	+ 2.1
Norway	+ 1.7	Jun	+ 0.4	na	na	+ 2.8	Jun	–15.8	+ 5.3	Q1	+ 4.6
Portugal	+ 3.7	May	+ 3.3	na	na	+ 1.1	May	+ 0.6	+ 1.1	Apr	+ 0.1

*New series.

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Portfolio poll

Jul 10th 2003
From The Economist print edition

Portfolio poll

▼▲ A change of 5% points or more on previous quarter
▼▲ A change of less than 5% points on previous quarter

	Holdings by instrument, %			Equity holdings by area, %						
	Equities	Bonds	Cash	United States	Other Americas	Britain	Euro area	Other Europe	Japan	Other Asia
Robeco Group	53	47	0	57	3	11	13	4 ▼	9 ▲	3
Julius Baer PB	40 ▼	42	18† ▲	47 ▼	5 ▲	5 ▼	10 ▼	9 ▼	12 ▲	12 ▲
Commerz Int. CM	56	44	0	41 ▼	2	5 ▼	31 ▲	3 ▼	17 ▲	1 ▼
Credit Suisse PB	35	35 ▼	30† ▲	69 ▲	0	0	16	0	4	11 ▼
Lehman Brothers	70	30	0	42 ▼	0	13 ▲	25 ▲	0 ▼	13 ▲	7 ▲
Standard Life	55	45	0	58 ▲	3 ▲	12	12 ▲	3 ▼	8 ▼	4 ▲
Daiwa IR	60 ▲	34	6 ▼	53 ▼	3	13 ▲	11	5 ▼	10 ▲	5 ▲
Average	53	39 ▼	8 ▲	53 ▼	2	8 ▼	17 ▲	3 ▼	10 ▲	6 ▲
Neutral*				57	3	11	14 ▲	4	8 ▼	3

	Bond holdings by currency, %				
	Dollar	Yen	Sterling	Euro area	Others
Robeco Group	3 ▼	35 ▲	9 ▲	51 ▲	2 ▼
Julius Baer PB	88	0	0	7	5
Commerz Int. CM	40 ▲	10 ▼	8 ▲	37 ▲	5 ▲
Credit Suisse PB	87 ▲	4 ▲	0 ▼	9 ▼	0
Lehman Brothers	43 ▼	17 ▼	4	32 ▲	4 ▲
Standard Life	22 ▼	27 ▼	4 ▼	43 ▲	4 ▲
Daiwa IR	27 ▲	16 ▼	5	45	7 ▲
Average	44	16 ▼	4 ▼	32 ▲	4
Neutral*	21 ▼	28 ▼	5	41 ▲	5

*Morgan Stanley Capital International (developed) world equity index; Citigroup world government-bond index

†Of which 8% invested in alternative investments

‡Of which 20% invested in alternative investments

In the second quarter of 2003, fund managers in our poll remained cautious, despite the end of the war in Iraq and the rally in equity markets. Only Daiwa increased its equity holdings. Our moneymen also pulled back from corporate America; only Credit Suisse and Standard Life increased their positions in American shares from the previous quarter. The euro area was more popular with our fund managers, whereas nearly all of them sold shares in European companies based outside the single-currency area. And, although the dollar remains weak, Commerzbank, Credit Suisse and Daiwa still found dollar-denominated bonds attractive. Bets on bonds denominated in euros proved widely popular, but only two managers increased their stakes in bonds paying out in yen or sterling.

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Money and interest rates

Jul 10th 2003
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Jul 9th 2003)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 4.7	+11.6	May	4.73	4.95	4.45	5.11	5.95	5.85
Britain	+ 7.9	+ 8.3	May	3.53	4.03	3.28	4.29	5.04	5.76
Canada	+10.3	+ 7.1	May	3.10	2.85	3.16	4.71	5.41	6.32
Denmark	+ 9.7	+12.2	May	2.25	3.75	2.15	4.07	5.13	5.32
Japan	+ 4.7	+ 1.8	Jun	0.01	0.03	0.08	1.09	1.29	1.23
Sweden	+ 4.0	+ 7.1	May	2.69	4.29	2.85	4.25	5.36	3.36
Switzerland	+27.6	+10.6	May	0.27	1.18	0.30	2.33	3.08	3.13
United States	+ 6.4	+ 6.6	May	1.08	1.76	1.35	3.70	4.64	5.32
Euro area†	+11.4	+ 8.5	May	2.13	3.42	2.13	3.87	4.87	3.86

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.58%, Japan No.250 1.11%. Central bank rates: US fed funds 1.00%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 3.75%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Jul 10th 2003
From The Economist print edition

1995=100

	Jul 1st	Jul 8th*	% change on one month	% change on one year
Dollar index				
All items	76.0	76.4	– 1.4	+ 4.4
Food	76.3	76.3	– 2.9	+ 2.5
Industrials				
All	75.6	76.5	+ 0.7	+ 7.1
Nfa†	79.9	79.8	+ 2.2	+ 9.2
Metals	71.9	73.7	– 0.6	+ 5.3
Sterling index				
All items	72.1	73.7	– 0.6	– 1.2
Euro index				
All items	86.2	88.9	+ 2.0	– 8.2
Yen index				
All items	96.4	96.2	– 0.8	+ 4.5
Gold				
$ per oz	351.80	344.30	– 2.6	+ 9.7
West Texas Intermediate				
$ per barrel	30.14	30.24	– 4.5	+15.8

* Provisional. † Non-food agriculturals.

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Stockmarkets

Jul 10th 2003
From The Economist print edition

Market indices

	Jul 9th	2003 high	2003 low	% change on one week	% change on record high	% change on Dec 31st 2002 in local currency	% change on Dec 31st 2002 in $ terms
Australia (All Ordinaries)	3,008.3	3,077.0	2,673.3	+ 0.2	-12.5	+ 1.1	+17.5
Austria (ATX)	1,330.9	1,343.0	1,120.2	- 0.1	-23.4	+15.7	+24.9
Belgium (Bel 20)	1,965.8	2,074.1	1,426.6	+ 1.8	-46.6	- 2.9	+ 4.7
Britain (FTSE 100)	4,054.7	4,207.0	3,287.0	+ 1.2	-41.5	+ 2.9	+ 4.2
Canada (Toronto Composite)	7,117.3	7,121.0	6,228.6	+ 1.8	-37.5	+ 7.6	+23.5
Denmark (KBX)	183.5	188.8	145.0	- 0.7	-39.2	+10.4	+19.0
France (SBF 250)	2,122.3	2,154.5	1,630.1	+ 2.2	-51.7	+ 3.4	+11.5
(CAC 40)	3,139.9	3,213.9	2,403.0	+ 2.0	-54.6	+ 2.5	+10.6
Germany (DAX)	3,322.4	3,344.5	2,203.0	+ 2.5	-58.8	+14.9	+23.9
Italy (BCI)	1,162.0	1,195.9	959.4	+ 1.7	-46.8	+ 6.4	+14.8
Japan (Nikkei 225)	9,991.0	9,991.0	7,607.9	+ 4.2	-74.3	+16.5	+17.4
(Topix)	979.4	979.4	770.6	+ 3.6	-66.1	+16.1	+17.0
Netherlands (AEX)	302.6	337.3	218.4	+ 2.8	-56.9	- 6.3	+ 1.2
Spain (Madrid SE)	726.6	737.3	576.8	+ 1.3	-36.6	+14.6	+23.7
Sweden (Affarsvarlden Gen)	160.6	162.0	127.8	+ 3.3	-59.9	+10.6	+19.3
Switzerland (Swiss Market)	4,869.0	4,992.5	3,675.4	+ 1.7	-42.1	+ 5.1	+ 6.5
United States (DJIA)	9,156.2	9,323.0	7,524.1	+ 0.1	-21.9	+ 9.8	+ 9.8
(S&P 500)	1,002.2	1,011.7	800.7	+ 0.8	-34.4	+13.9	+13.9
(NASDAQ Comp)	1,747.5	1,747.5	1,271.5	+ 4.1	-65.4	+30.8	+30.8
Europe (FTSE Eurotop 300)*	863.3	890.8	682.7	+ 1.8	-49.4	+ 0.7	+ 8.7
Euro area (FTSE Ebloc 100)*	745.3	758.6	565.7	+ 2.2	-51.9	+ 3.7	+11.9
World (MSCI)†	894.8	907.3	710.8	+ 1.0	-38.2	na	+12.9
World bond market (Citigroup)‡	558.1	583.9	518.6	- 1.1	- 4.4	na	+ 6.2

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms. ‡Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Jul 10th 2003
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current account $bn latest 12 mths		Current account % of GDP, forecast 2003	Current account % of GDP, forecast 2004	Exchange rate trade-weighted† 1990=100 Jul 9th	Exchange rate trade-weighted† 1990=100 year ago	Currency units per $ Jul 9th	Currency units per $ year ago	Currency units per £	Currency units per euro	Currency units per ¥100	Budget balance % of GDP 2003‡
Australia	− 9.5	May	− 20.8	Q1	− 5.1	− 4.3	82.1	74.9	1.53	1.77	2.49	1.73	1.30	0.2
Austria	+ 0.7	Mar	+ 1.7	Apr	+ 0.1	nil	103.0§	100.4	0.88	1.01	1.44	–	0.75	-1.3
Belgium	+ 17.3	Apr	+ 11.1	Feb	+ 4.7	+ 4.7	103.3§	99.4	0.88	1.01	1.44	–	0.75	nil
Britain	− 73.7	May	− 5.8	Q1	− 1.4	− 1.4	100.0	105.1	0.61	0.65	–	0.69	0.52	-1.9
Canada	+ 36.2	Apr	+ 13.9	Q1	+ 1.8	+ 1.5	85.0	78.0	1.38	1.52	2.24	1.56	1.17	1.1
Denmark	+ 9.2	Apr	+ 5.7	Apr	+ 2.6	+ 2.3	106.2	103.2	6.57	7.52	10.7	7.44	5.58	1.6
France	+ 7.4	Apr	+ 25.3	Apr	+ 1.7	+ 1.6	106.8§	102.1	0.88	1.01	1.44	–	0.75	-3.6
Germany	+127.3	May	+ 49.7	May	+ 2.1	+ 1.9	104.4§	98.9	0.88	1.01	1.44	–	0.75	-3.7
Italy	+ 5.4	Apr	− 12.3	Apr	− 0.5	− 0.5	76.1§	72.8	0.88	1.01	1.44	–	0.75	-2.4
Japan	+ 96.9	May	+114.9	May	+ 2.2	+ 2.4	129.7	136.7	118	118	192	133	–	-7.7
Netherlands	+ 29.5	Apr	+ 2.9	Q1	+ 2.5	+ 2.7	102.8§	98.4	0.88	1.01	1.44	–	0.75	-1.6
Spain	− 44.4	Apr	− 19.8	Mar	− 2.3	− 2.3	77.3§	74.5	0.88	1.01	1.44	–	0.75	-0.4
Sweden	+ 15.7	May	+ 11.5	Q1	+ 3.5	+ 3.3	80.6	76.4	8.08	9.40	13.2	9.15	6.86	0.7
Switzerland	+ 5.5	May	+ 32.8	Q1	+11.6	+11.3	111.6	113.8	1.36	1.49	2.22	1.55	1.16	na
United States	−519.7	Apr	−510.2	Q1	− 5.3	− 5.5	103.6	112.0	–	–	1.63	1.13	0.85	-4.6
Euro area	+ 85.8	Apr	+ 44.1	Apr	+ 0.7	+ 0.6	89.6	81.9	0.88	1.01	1.44	–	0.75	-2.5
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 13.4	Apr	+ 9.3	Apr	na	na	82.2§	78.5	0.86	1.01	1.40	–	0.73	3.1
Greece	− 23.0	Apr	− 11.0	Apr	na	na	59.7§	57.7	0.85	1.01	1.40	–	0.73	-1.0
Iceland	nil	May	nil	Q1	na	na	97.2**	86.2	76.5	86.2	125	86.6	65.0	nil
Ireland	+ 36.8	Apr	− 0.2	Q4	na	na	95.5§	88.1	0.86	1.01	1.40	–	0.73	-0.8
Luxembourg	− 3.2	Apr	+ 1.7	Q4	na	na	103.3§	99.4	0.86	1.01	1.40	–	0.73	0.2
New Zealand	− 1.1	May	− 1.4	Q1	na	na	99.4	88.4	1.68	2.04	2.74	1.90	1.43	0.8
Norway	+ 27.8	May	+ 25.7	Apr	na	na	96.6	106.8	7.16	7.38	11.7	8.11	6.08	11.3
Portugal	− 12.5	Mar	− 8.1	Mar	na	na	92.7**	89.9	0.86	1.01	1.40	–	0.73	-3.2

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, May average. ‡OECD forecast. **IMF, March average.

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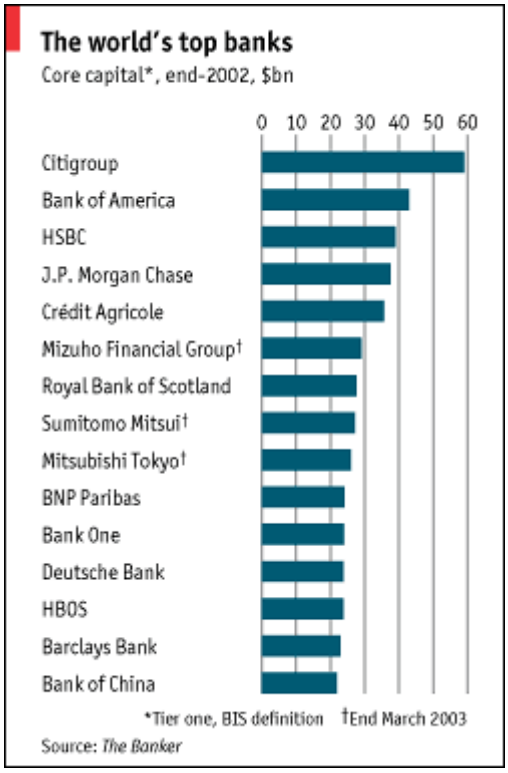
The world's top banks

Jul 10th 2003
From The Economist print edition



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Overview

Jul 10th 2003
From The Economist print edition

Malaysia's industrial production grew by 16.2% in the 12 months to May.

Argentina's GDP growth in the year to the first quarter was revised downwards slightly to 5.1%, from the earlier estimate of 5.4%.

Venezuela's manufacturing suffered in the 12 months to April. Thanks to civil strife, industrial output fell by 14.6%. **Colombia's** industrial output declined by 3.3% over the same period.

Taiwan recorded consumer-price deflation of 0.4% in the 12 months to June.

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Economic freedom

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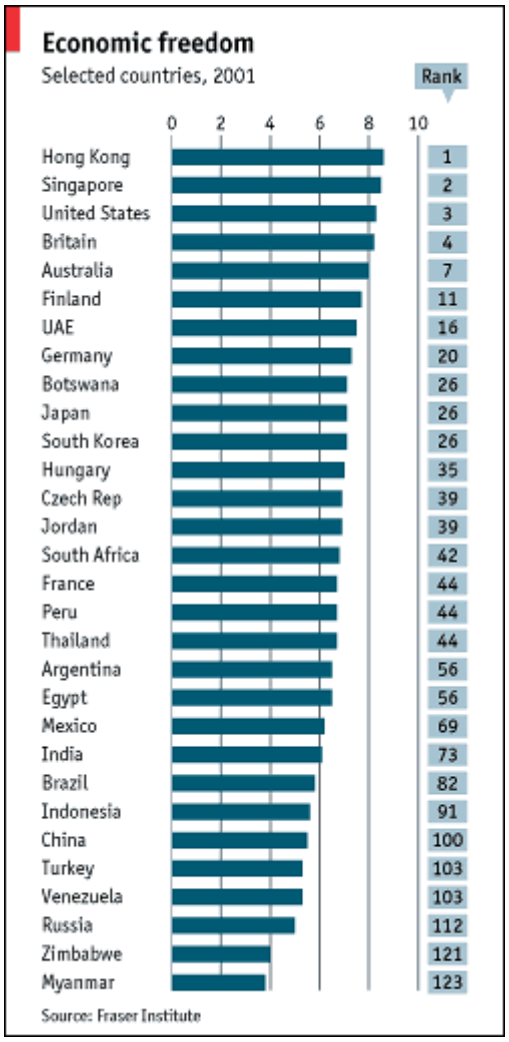
The Economic Freedom of the World index, created by the Fraser Institute, a Canadian think-tank, measures how consistent countries' policies are with economic freedoms, including personal choice, competition and property rights. In this year's report Hong Kong was still the most economically free country of the 123 surveyed. The least free countries are found in the Middle East, Africa and Latin America. The Fraser Institute says that economic freedom is highly correlated with the human-development index, as measured by the United Nations.



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Economy

Jul 10th 2003
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	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.9	Q1	+16.9	Jun	+ 0.7	May	+21.5	Jun	+35.4	2002	331.1	Apr
Hong Kong	+ 4.5	Q1	– 8.8	Q1	– 2.5	May	– 7.6	May	+18.4	Q1	114.4	Jun
India	+ 4.9	Q1	+ 4.9	Apr	+ 4.7	May	–10.6	May	+ 4.8	Q4	78.2	Jun
Indonesia	+ 3.4	Q1	+18.4	Mar	+ 6.6	Jun	+25.3	May	+ 7.5	Q4	33.0	May
Malaysia	+ 4.0	Q1	+16.2	May	+ 1.0	May	+16.3	May	+ 8.5	Q1	35.4	May
Philippines	+ 4.5	Q1	+ 2.0	Apr	+ 3.4	Jun	– 0.1	Apr	+ 2.9	Mar	12.7	Jun
Singapore	– 4.3	Q2	– 9.5	May	– 0.1	May	+12.3	May	+21.3	Q1	86.6	Jun
South Korea	+ 3.7	Q1	– 1.9	May	+ 3.0	Jun	+ 8.8	Jun	+ 2.7	May	128.3	May
Taiwan	+ 3.2	Q1	– 2.8	May	– 0.4	Jun	+16.4	Jun	+25.9	Q1	175.2	May
Thailand	+ 6.7	Q1	+12.8	May	+ 1.7	Jun	+ 4.3	May	+ 8.3	May	38.3	Jun
Argentina	+ 5.1	Q1	+12.2	May	+10.2	Jun	+17.0	May	+10.2	Q1	12.2	Jun
Brazil	+ 2.0	Q1	– 0.3	May	+16.6	Jun	+20.9	Jun	– 0.6	May	43.4	May
Chile	+ 3.5	Q1	+ 4.0	May	+ 3.6	Jun	+ 2.4	May	– 0.6	Q1	15.9	May
Colombia	+ 3.8	Q1	– 3.3	Apr	+ 7.2	Jun	– 0.4	Feb	– 1.6	Q4	10.6	May
Mexico	+ 2.3	Q1	– 4.8	Apr	+ 4.3	Jun	– 6.6	May	–12.7	Q1	53.6	May
Peru	+ 2.5	Apr	– 0.5	Apr	+ 2.2	Jun	+ 0.4	Apr	– 1.1	Q1	9.7	May
Venezuela	–29.0	Q1	–14.6	Apr	+34.2	Jun	+15.0	Q1	+ 9.5	Q1	10.5	Apr
Egypt	+ 3.1	2002†	+ 4.2	2002†	+ 3.7	Apr	– 7.4	Jan	+ 1.0	Q1	13.1	Feb
Israel	+ 0.3	Q1	– 2.4	Apr	+ 1.6	May	– 5.6	May	– 0.5	Q1	24.5	Jun
South Africa	+ 2.5	Q1	– 4.0	May	+ 7.8	May	+ 3.2	May	– 0.2	Q1	6.0	May
Turkey	+ 8.1	Q1	+ 4.8	May	+29.8	Jun	–14.0	May	– 3.3	Apr	28.6	May
Czech Republic	+ 2.2	Q1	+ 3.2	May	+ 0.3	Jun	– 2.3	May	– 4.4	Q1	25.6	Jun
Hungary	+ 2.7	Q1	+ 3.7	May	+ 3.6	May	– 2.8	Apr‡	– 3.6	Apr	12.4	Jun
Poland	+ 2.2	Q1	+11.7	May	+ 0.4	May	–10.2	May	– 5.6	May	32.3	May
Russia	+ 5.2	Q4	+ 8.5	May	+14.0	Jun	+52.6	May	+38.3	Q1	60.7	Jun
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Pakistan	+ 3.6	2002†	+15.8	Nov	+ 2.6	May	– 1.2	Jun	+ 2.6	2002†	9.7	Apr
Saudi Arabia	+ 0.7	2002§	na		– 1.5	Apr	+38.6	2002§	+11.7	2002	23.1	Apr

*Excluding gold, except Singapore; IMF definition. †Year ending June. ‡New series. §Economist Intelligence Unit estimate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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Financial markets

Jul 10th 2003
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Jul 9th		Dec 31st 2002	
	Jul 9th	year ago	Jul 9th	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	13.5	na	1,574.4	+0.3	+ 10.9	+ 10.9
Hong Kong	7.80	7.80	12.7	1.12	10,027.4	+4.4	+ 7.6	+ 7.6
India	46.2	48.8	75.3	5.02	3,620.8	+0.5	+ 7.2	+ 11.2
Indonesia	8,196	8,908	13,357	10.01	519.8	+2.7	+ 22.3	+ 33.6
Malaysia	3.80	3.80	6.19	3.10	725.7	+3.2	+ 12.3	+ 12.3
Philippines	53.4	50.2	87.0	8.38	1,295.5	+5.5	+ 27.2	+ 27.2
Singapore	1.75	1.75	2.85	0.56	1,523.2	+3.1	+ 13.6	+ 12.7
South Korea	1,179	1,169	1,922	4.34	705.5	+2.9	+ 12.4	+ 13.1
Taiwan	34.3	33.1	55.9	1.10	5,358.9	+5.2	+ 20.4	+ 22.0
Thailand	41.7	41.2	67.9	1.29	482.5	+1.0	+ 35.4	+ 40.1
Argentina	2.77	3.52	4.52	10.81	721.2	−3.7	+ 37.4	+ 66.7
Brazil	2.87	2.86	4.67	25.76	13,618.8	+2.3	+ 20.9	+ 49.2
Chile	704	699	1,147	2.76	6,039.4	−0.2	+ 20.3	+ 23.1
Colombia	2,849	2,482	4,643	7.81	2,203.3	+5.8	+ 37.0	+ 37.8
Mexico	10.49	9.83	17.1	4.91	7,171.9	+0.1	+ 17.1	+ 16.8
Peru	3.47	3.54	5.66	3.54	1,852.5	+0.8	+ 33.1	+ 34.7
Venezuela	1,598	1,316	2,604	17.83	14,569.0	+5.6	+ 81.8	+ 57.7
Egypt	6.06	4.63	9.87	10.27	9,036.1	+6.7	+ 68.2	+ 28.6
Israel	4.32	4.71	7.04	4.58	444.0	−3.3	+ 33.5	+ 46.8
South Africa	7.6	10.0	12.4	11.60	8,629.1	+2.8	− 7.0	+ 5.0
Turkey	1,420,500	1,662,500	2,315,131	37.00	10,364.9	−3.0	− 0.0	+ 16.8
Czech Republic	27.9	29.3	45.5	2.25	542.7	+0.7	+ 17.8	+ 27.0
Hungary	232	253	378	9.49	8,076.8	+2.5	+ 3.6	+ 0.3
Poland	3.93	4.16	6.40	5.25	16,893.0	+6.1	+ 17.6	+ 14.7
Russia	30.4	31.6	49.5	16.00	493.8‡	−4.7	+ 30.8	+ 37.5
EMF (MSCI)*	1.00	1.00	1.63	na	349.7	+2.5	na	+ 19.7
EMBI+†	1.00	1.00	1.63	na	269.4	−2.1	na	+ 17.7
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Pakistan								
Saudi Arabia								

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡ In $ terms.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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